

October 19, 2021

RESPONSIBLE INVESTING

ILPA ESG Resources: Iterative Roadmap Can Help LPs in Early Integration Stages (Part Two of Two)

By Helen Kim, *Private Equity Law Report*

The Institutional Limited Partners Association (ILPA) has produced numerous resources for LPs over the years. Recently, it has bulked up its offerings related to environmental, social and governance (ESG) issues, including releasing an ESG Roadmap and Resources in May 2021 for LPs embarking on ESG integration internally. ILPA also released an [ESG Assessment Framework](#) (Framework) in July 2021 to help LPs assess GPs' integration of ESG principles.

The Private Equity Law Report interviewed a number of industry experts to analyze the potential impact of ILPA's ESG resources. This second article in a two-part series analyzes the ESG Roadmap and Resources, as well as other ESG resources offered by ILPA and their potential impact on the PE industry. The [first article](#) provided an overview of how key features of the Framework can benefit both LPs and GPs, while also speculating on the scope of its adoption.

See our two-part series on revisions to ILPA's model limited partnership agreement: "[Analysis and Market Response to ILPA's Deal-by-Deal Waterfall Model LPA](#)" (Sep. 15, 2020); and

"[Clarifying Updates to Non-Economic Provisions in ILPA's Model LPA](#)" (Sep. 22, 2020).

ESG Roadmap

The ESG Roadmap and Resources is a page on ILPA's website that provides ESG-related resources to LPs based on specific actions LPs can take when building their internal ESG programs. The page "is intended to be a clearinghouse of best practices and resources that reflects the ongoing development and evolution of successful ESG in LP organizations."

The Roadmap sets out five major categories of integration:

1. organizational policy and infrastructure;
2. due diligence and investment decision making;
3. managing GP relationships;
4. reporting and benchmarking; and
5. internal and external communications.

Each category contains up to five sub-categories which lead to resources from various organizations.

Under the reporting and benchmarking category, for example, the two sub-categories are:

1. identify, request and monitor ESG-specific key performance indicators (KPIs), which provides links to:
 - ILPA's portfolio company metrics template;
 - the United Nations' Principles for Responsible Investment (PRI) guidance on ESG-specific KPIs;
 - the standards of the Sustainability Accounting Standards Board (SASB);
 - SASB's materiality map; and
 - a report by the European Federation of Financial Analysts Societies; and
2. encourage GPs to report on ESG performance at the firm level on a quantitative and qualitative basis, which provides links to KKR's 2018 ESG, Impact and Citizenship Report and LGT Capital Partners' 2019 ESG report.

Currently, the only subcategory without any resources is "Leverage seat on an [LP advisory committee] (when applicable) to influence ESG matters," under the managing GP relationships category.

ILPA encourages submissions of resources on the site. "Anyone who is interested can submit publicly available resources that are useful and informative for further consideration," said Matthew D. Schey, ILPA's senior director of strategic projects. ILPA has received samples of LP policies, white papers and other submissions through the viewer submission button.

Process of Creation and Release

The Roadmap began as a series of conversations with ILPA members about their ESG journeys, Schey recalled. "We learned more about their current ESG programs and asked specifically about the steps and actions they took to get there." The responses were considered for effectiveness, usefulness and commonality, with ILPA then searching for the best examples of activities in action (e.g., a sample policy or report). "Is it practical? Is it widely used and well known? Is it going to help someone trying to make this step a reality?" he explained.

ILPA initially released the Roadmap in early 2020 only to its members but decided to release it publicly in May 2021. "The initial goal was to help ILPA members identify steps toward integrating ESG considerations into their investment programs and pair those actions with real life examples," Schey explained. "When it comes to topics like ESG and diversity, equity and inclusion (DEI), however, we want the entire industry to have access to resources and to participate in dialogue."

ILPA plans to continue to invest in and update the Roadmap and Resources in the future, Schey continued. "It is meant to provide a menu of options that other LPs have taken and found success with, while acknowledging that different LPs will emphasize different things."

See our four-part series on diversity: "[Why Equal Representation Within Fund Managers Is Essential](#)" (Oct. 4, 2018); "[Ways Fund Managers Can Promote Diversity and Inclusion](#)"

(Oct. 11, 2018); “[What Implicit Biases Are and Whether Interventions Are Effective](#)” (Oct. 18, 2018); and “[How Constrained Decision Making, Along with Legal and Compliance Leadership, Can Help Reduce Fund Manager Bias](#)” (Nov. 1, 2018).

Which LPs Can Benefit From the Roadmap

The Roadmap is a good starting point for LPs whose ESG programs are in the early stages of development or are expanding, Schey advised. “It’s one of the first places we point our members who are interested in learning and doing more in the area of ESG,” he said. “It’s a great resource for an LP whose board or chief investment officer has indicated an interest in integrating ESG in the investment thesis. It sets out some things an LP needs to do on the private market side to make that a reality.”

The Roadmap looks like what it is meant to be – a work in progress. “Having an evolving roadmap and set of resources makes a lot of sense,” said Reed Smith partner Shervin Shameli, who represents both LPs and GPs. “The resources provide very useful information for LPs forming their best practices and gives them an opportunity to see what others are doing in the industry.”

LPs that are new to PE, some family offices and LPs that tend not to be in touch with other LPs may find the Roadmap helpful for thinking about what they need to factor into their ESG programs, Shameli suggested. Conversely, a large institutional investor that has already built a considerable internal ESG program may find the Roadmap less useful. “I suspect those LPs have already ticked most of the boxes already,” he said. “It can be helpful, however, for even those LPs to see what others are doing.”

How GPs Can Use the Roadmap

While the Framework can help GPs understand LP expectations, the Roadmap can help GPs understand what LPs are doing internally, Schey suggested. “Although we wrote the Roadmap from an LP perspective, it provides a good opportunity for GPs to take a look at the types of actions LPs are taking,” he said. “There are numerous reasons why a GP might be looking to prioritize ESG integration. Some see it as a value-creation lever while others may be responding to investor requirements. GPs in the latter camp can use the Roadmap to better understand those investor requirements.”

Many resources may be familiar to both GPs and LPs, such as PRI and SASB, said Kirkland & Ellis partner Mary Beth Houlihan, who advises sponsors on ESG issues. “Most of our clients have fairly sophisticated ESG programs already,” agreed Kirkland & Ellis partner Nadia Murad, who advises mostly GPs. “But, the Roadmap could be a useful tool for a GP seeking to enhance its ESG program,” she clarified. Although many of the resources are publicly available, it is helpful having them categorized and available in one central location, Shameli added.

In addition, because ESG is an evolving area, the Roadmap and Resources can be useful to both GPs that are starting their ESG integration as well as those that have a sophisticated program. “If a GP can keep on top of what LPs consider ESG best practices and cross-check some of the resources provided, it can evolve and align itself with LP expectations,” Shameli advised. “There are always improvements and tweaks that can be made.”

See “[Emerging Trends in LP Demands for Standardized ESG Reporting and How GPs Have Attempted to Comply](#)” (Jul. 20, 2021).

GP-Side Responses

On a standalone basis, the Roadmap is light on detail, Shameli said. “It may be meant to be light, however, as I don’t think ILPA is necessarily missing anything,” he posited. “But, taken together with the Resources and Framework, the details are there. I recommend LPs, GPs and those who advise them to take a look at those resources.”

For instance, he continued, the section on organizational policy and infrastructure is missing considerations around training the investment team on ESG issues. “It is captured in the Framework, but it is omitted as a line item under that heading of the Roadmap.” Similarly, the section on reporting and benchmarking does not specifically address incident reporting and remedial measures that should be part of addressing problems at portfolio companies, but the Framework does contain some details around those actions.

Other experts sought additional definitions as well. “I would have defined what ‘qualitative’ and ‘quantitative’ mean, as well as offered some guidance on what standards to apply and how to benchmark,” said Morrison & Foerster partner Susan H. Mac Cormac. “In term of portfolio companies, benchmarking is what has been missing to date in funds’ ESG work. How a fund and its portfolio companies are doing on their KPIs compared to other funds and their portfolio companies is missing in most GP analysis,” she said.

In addition, lack of standardization in KPIs can lead to incomplete information. For example, a GP investing in renewable energy in Africa may

be aware of and measuring the emissions reduction associated with renewable energy, but not be aware of the materials with which the renewable energy resource was built. “The portfolio company could be using carbon-sequestering cement,” Mac Cormac suggested, which could boost the ESG quotient of the investment.

Schey acknowledged the desire for benchmarking from the LP side. “Lately, we are hearing a need for more resources specific to KPIs and reporting,” he said. “That’s an area we will be focusing on because LPs and GPs alike are asking for more guidance about best practices.”

See “[Adoption of ESG Voluntary Standards By Fund Managers to Overcome U.S. Regulatory Shortcomings and Bolster ESG Defensibility \(Part Two of Two\)](#)” (Jun. 1, 2021).

Other ILPA ESG Resources

ILPA recently released a revised version of its Due Diligence Questionnaire (DDQ) for public comment that includes expanded ESG and DEI sections. As in 2018, ILPA and PRI worked together to incorporate PRI’s recently updated questions on ESG into the ILPA DDQ in the hopes of increasing efficiencies for LPs and GPs.

ILPA drew on insights from its Diversity In Action initiative – launched in 2020 and focused on motivating market participants to become more diverse and inclusive – to inform changes to the DEI section and its Diversity Metrics Template, which is also out for public comment.

“The enhanced DDQ reflects market trends,” Murad observed. “Our clients have been more proactive in providing information and

disclosure on ESG and DEI issues while investors have requested more information in their diligence.” Collecting information on DEI can be challenging, however, for GPs and portfolio companies that operate in jurisdictions with strong data privacy issues, Houlihan pointed out.

“Many of our clients use the ILPA DDQ, so I would expect to see any updates get integrated into the overall process,” Murad predicted. A number of Shameli’s LP clients also use the ILPA DDQ and he agreed that it serves as a good benchmark for GPs as well. “ILPA is always a good starting point because many LPs will use ILPA forms and guidance to create their own DDQs. A GP will generally have a fairly comprehensive DDQ that is more balanced than the ILPA form.”

In July 2021, ILPA also began to offer online ESG courses to its members. The initial response has been positive, Schey reported.

For more on other areas of ILPA guidance, see “[Trends in PE Funds’ Core Economic Terms and Adoption of Recent ILPA Recommendations](#)” (Sep. 24, 2019); and “[ILPA Makes Recommendations for LPs Participating in GP-Led Secondary Fund Restructurings](#)” (Jul. 9, 2019).

Impact on Industry

Overall, the resources are helpful and attempt to be responsive to the market and what LPs and GPs need, Houlihan said. Shameli agreed, “The resources help make the industry more transparent and informed.” It is hard, however, to predict the influence the Framework and Roadmap may have on the PE industry, in part because individual LPs and GPs have different investment restrictions and policies.

To date, most of the experts interviewed by the Private Equity Law Report have not seen much market activity or discussion around the Framework or Roadmap. “I don’t think they’ve influenced investor negotiations or decisions to date, but they are relatively new,” Murad noted. “If LPs increasingly use the Framework, however, it could be very useful for people to coalesce around,” Houlihan suggested.

ILPA is the first to acknowledge, however, there is room to improve the ESG resources. For example, as the Framework was developed with mid- to large-cap buyout managers in mind, ILPA recognized the need for further guidance in other private markets areas such as real estate, private credit, venture capital and infrastructure, according to Schey. “ILPA is considering what supplementary additions to its Framework addressing other private markets asset classes could look like,” he added.

In addition, ILPA will be focusing on KPIs and reporting going forward. “A number of different standard setters, industry groups and organizations are looking to tackle that challenge,” Schey said. “Coming up with an industry-led, globally harmonized approach is going to be absolutely key.” He emphasized that ILPA welcomes dialogue from LPs, GPs and service providers. “This is an area where collaboration across the industry is critical. You don’t have to be an ILPA member to reach out and have a conversation with us on any of these topics.”

See “[LPs Are Increasingly Frustrated by GPs’ Outdated Technology and Non-Standardized Reporting](#)” (Dec. 15, 2020).