SWIB STATE OF WISCONSIN INVESTMENT BOARD

VIA EMAIL

January 31, 2019

Hon. W. Jay Clayton, Chairman
Hon. Robert J. Jackson Jr., Commissioner
Hon. Hester M. Peirce, Commissioner
United States Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549-1090

RE: Public Comments from Interested Parties on MiFID II's Research Provisions

Dear Commissioners:

The State of Wisconsin Investment Board ("SWIB") has assets under management of approximately $110 billion[1] and is responsible for managing the assets of the Wisconsin Retirement System, the 8th largest public pension plan in the United States, and other state funds. SWIB is a fiduciary, managing plan assets for over 622,000 individuals who participate in the plan and for over 1,500 Wisconsin employers who contribute on behalf of their employees. Plan participants are teachers, police and firefighters, state university employees and other state and local government employees. At SWIB, we use our own investment staff to internally manage over half of the assets under management and directly use sell-side research in our investment management process.

We are writing in response to the request for comment from market participants on the impact the European Union's (EU's) Markets in Financial Instruments Directive (MiFID II)'s research provisions to share how such provisions and the related no-action letters affect SWIB.

Background

We believe there are significant differences between a pension plan managing assets for a plan and an investment adviser managing assets for clients. Unlike an investment adviser, with respect to the plan, there is no distinction between client assets and the adviser's assets or profit & loss (P&L) statement. All plan expenses come from the same pool of assets. Therefore, whether we pay for research through

[1] As of December 31, 2018.

commissions or by hard dollar payments, the funds all come from the same source, which is the pension plan assets we manage.

As a fiduciary, our investment management teams are responsible for managing research budgets in a way that fairly allocates expenditures for research to the investment teams that use the research and to pay only reasonable value for the research received. Paying for research through bundled commission payments makes it extremely challenging to allocate costs to the investment teams using the research, results in varying levels of research payments year-over-year driven by trading volumes rather than the quality of the research received, does not allow for transparency in accurately reporting the research expenditures versus execution costs and makes it very difficult to assess the value and quality of the research received for the commission dollars paid for such research.

As a world-class public pension plan and fiduciary, our internal investment teams use and evaluate the research provided to develop their own investment theses for the investment decisions they make and do not rely on the research received as "investment advice".

<u>No-Action Letter</u>

As a result of the SEC's SIFMA no-action letter[2], a conflict has been created between EU and non-EU investors and EU and non-EU money managers. Consequently, EU asset owners and clients are treated differently than U.S. asset owners and clients. As a U.S.-based public pension plan and asset owner, SWIB is not subject to MiFID II nor contractually required to comply with MiFID II. Because registered broker-dealers are concerned about being required to register as an investment adviser under the current regulatory landscape, U.S. pension plans, like SWIB, may be forced to pay for research through a commission-based payment rather than simply writing a hard dollar check, or cease obtaining research from such firms. On the other hand, under the SIFMA no-action letter, a public pension plan in the EU would be permitted to write a check to a U.S. broker-dealer for the same research. This result disadvantages U.S. clients, like SWIB, in that it limits access to research from some of the largest broker-dealers. As a fiduciary, we want to focus on achieving best execution for the plan and other funds that we manage while obtaining quality research for a reasonable price and allowing transparency into both our cost of execution and our cost of research.

<u>Recommendation</u>

We support the positions set forth in the MFS Comment letter dated October 16, 2018 to end the artificial distinctions and inherent conflict created between EU and non-EU investors and money managers and allow flexibility in structuring payments to broker-dealers for research through either hard or soft dollars. We urge the SEC to take prompt action to cure these conflicts created and not wait until expiration of the no-action letter in July 2020. Until these conflicts are cured, SWIB, and others asset owners like SWIB, may be forced to forego obtaining valuable research used in the investment management process, or

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[2] Securities Industry and Financial Markets Association, SEC Staff No-Action Letter (pub. avail. Oct. 26, 2017).

continue to pay through the far more challenging and less transparent commission generation and payment process.

As a U.S. pension plan and asset owner, we differ from both EU and non-EU investment advisers in that the source of payment for research is not a choice of client assets or adviser P&L. The source of payment is the same, the pension plan assets. As a fiduciary, the research received is not considered, nor do we treat it, as investment advice. There should be no difference whether we pay for research with soft or hard dollars.

On behalf of the over 622,000 participants in the Wisconsin Retirement System, we at the State of Wisconsin Investment Board thank you for the opportunity to comment on this issue. We appreciate the efforts of the staff to seek input from all types of market participants, and we are hopeful for a prompt and equitable solution to resolve these challenges.

Sincerely,

David Villa
Executive Director/Chief Investment Officer