U.S. SECURITIES AND EXCHANGE COMMISSION

MEETING OF THE

SECURITIES AND EXCHANGE COMMISSION

ASSET MANAGEMENT ADVISORY COMMITTEE

Via Webex Video Teleconference

Wednesday, September 16, 2020

U.S. Securities and Exchange Commission

100 F Street NE

Washington, D.C.

PARTICIPANTS:

Securities and Exchange Commission:
Jay Clayton, Chairman
Hester Peirce, Commissioner
Elad Roisman, Commissioner
Caroline Crenshaw, Commissioner
Dalia Blass, Director, Division of Investment Management

Panelists:
Cheryl Alston
Michael Frerichs
Anyori (A.J.) Hernandez
Bryan Jenkins
Clayton Jue
Josh Lerner
Michael Manning
Michael Miller
Noel O'Neil
Ludovic Phalippou

AMAC Members:
Ed Bernard, AMAC Committee Chairman
John Bajkowski
Michelle Beck, Panel Moderator

PARTICIPANTS(CONT.):

AMAC Members(cont.):
Jane Carten
Scot Draeger
Michael Durbin
Gilbert Garcia, Panel Moderator
Paul Greff
Richard Hall
Neesha Hathi
Adeel Jivraj
Ryan Ludt
Susan McGee
Jeffrey Ptak
Erik Sirri, Panel Moderator
Aye Soe
Ross Stevens
Rama Subramaniam
John Suydam
Russ Wermers
Alex Glass (non-voting)
Joe Savage (non-voting)

C O N T E N T S

C O N T E N T S (CONT.)

PROCEEDINGS

MR. BERNARD: Good morning. I'd like to call this meeting on September 16, 2020, of the Asset Management Advisory Committee meeting to order. Welcome to those of you joining on sec.gov. I would note that we have a quorum. This is a virtual meeting on Webex. And we've already done a sound check to ensure that all committee members and commissioners can hear. If there is any problems among those who are participating, please send a private text to Gabe Collins or Veronica Davis, and they will help us sort it out.

To open the meeting, I'd like to thank Chairman Clayton and Commissioners Peirce, Roisman and Crenshaw for their attendance with a special welcome to the most recent appointee, Commissioner Crenshaw, and invite each of them to offer any opening remarks they may have. Chairman Clayton?

CHAIRMAN CLAYTON: Thank you, Ed, and welcome, everyone, to today's meeting of the Commission's Asset Management Advisory Committee or, as we call it, the AMAC, including -- joining us virtually or listening to the meeting through the Commission's website. I'm very glad that the important work of the committee and, more broadly, the Commission has been able to continue virtually uninterrupted as we remain in our telework

posture. I'm very pleased to be joined today by several of my fellow commissioners. And Ed, as you mentioned, I'd like to welcome Commissioner Crenshaw, who is attending her first AMAC meeting as a commissioner.

Many of you likely worked with Commissioner Crenshaw during her career here at the SEC. Commissioners Peirce and Roisman, as Ed noted, are also joining as well. Before I discuss today's agenda, a number of thank yous are appropriate, first, everyone who has worked hard to make today's meeting productive and insightful. Thank you to the members of the committee, including Ed, for your continued leadership. It's greatly appreciated, Ed.

Thank you also to the committee members serving as today's panel moderators. And I'm proud to say I know both of them very well, Erik Sirri and Gilbert Garcia. Thank you to the Commission staff who have helped with today's meeting, including Director Dalia Blass and her staff and to all of the staff in our office of minority and women inclusion, including Robert Marchman, our senior adviser for diversity and inclusion. Robert, you're just doing a terrific job.

Thanks as always to the staff in the Office of Information Technology and the Office of the Secretary for your assistance. And thank you especially to the

panelists and others presenting during today's meeting for your time and your willingness to share your insights with the committee and with the Commission.

Today's agenda is full and reflects both the breadth of the Asset Management Advisory Committee's work and the depth of analysis that your structure allows. To that end, I look forward to presentations from two subcommittees, the ESG Subcommittee and the Private Investments Subcommittee. I understand that both subcommittees continue to make progress on the respective workstreams and will be able to provide updates to help inform the AMAC.

In addition, I welcome today's discussion on the impact of COVID-19 within the asset management industry, which is a follow-up to the conversation the committee began in May. Today's discussion should provide additional insight into these impacts with a particular focus on exchange-traded products and the industry's operations. The Commission and staff continue to monitor the effects of COVID-19 on our markets, including through our market monitoring group and our ongoing outreach to market participants.

And I appreciate the opportunity for additional feedback that this discussion will provide. I assure you that we are listening and we are adjusting

in light of your experiences. They greatly help us. Turning to today's panelists, I look forward to the panelists' presentation regarding private investment returns.

I've spoken on numerous occasions about my interest in promoting access and choice for Main Street investors, including ways we might increase their access to private markets while we ensure appropriate investor protections. As part of this, we should examine whether appropriately-structured funds can facilitate greater Main Street investor access to private investments, particularly as a component of an investor portfolio that is analogous to the portfolio of a well-managed pension fund.

We should make sure to focus on fees and investor protections. As I've said previously, one of the greatest things about our public markets is that they allow our Main Street investors to invest side by side with sophisticated and institutional investors in the same companies. I believe a similar result can be achieved through appropriately-structured funds.

The input from today's panelists will no doubt provide useful information for our efforts. I also welcome your continued discussions on improving diversity and inclusion in the asset management industry. The discussions held at your July meeting on this topic provided a stark, honest and very helpful analysis of the current state of diversity and inclusion in the asset management industry, including opportunities for diverse asset managers.

That meeting clarified further that there is significant support for our shared goal of expanding those opportunities and sustained interest in helping us determine how best we can achieve it. I'm hopeful that today's panelists will help to further consideration of this issue with an eye towards some of the best practices observed by consultants and professionally managed pension funds.

Thank you again to all of today's participants and attendees. The range of experience and perspectives that the Commission receives from the AMAC and our other advisory committees truly improves our regulatory decisions and enables us to benefit the investors and the markets that we serve. Thank you, Ed.

MR. BERNARD: Thank you, Commissioner Clayton or Chairman Clayton. Forgive me.

Commissioner Peirce?

COMMISSIONER PEIRCE: Thank you, Ed, and thanks to the members of the committee and to all of today's panelists. I'm looking forward to the

discussions. Just a couple comments on the diversity and inclusion panel. I think one thing we should think about is the role that regulation may play in excluding certain people from participating in this industry. I think we -- we heard about that at the Small Business Capital Formation Advisory Committee, where -- where the accredited investor threshold was cited as something that has kept people from participating in those markets.

And I think traditionally we've seen regulation can be a way to keep people out and to keep - to protect incumbents and to keep new entrants out. So maybe we can think about the role that regulation plays. And then second, I know you all have a very busy agenda, but I'd like to add another potential item for consideration which is prompted by last month's withdrawal of the Boulder no-action letter.

It would be interesting to hear from all of you what you think the implications of that will be for closed-end funds. And so I would -- I would love to hear that discussion at some point. Thank you. And I hope that you all have a wonderful day.

MR. BERNARD: Thank you, Commissioner Peirce.

Commissioner Roisman?

COMMISSIONER ROISMAN: Thank you, Ed. And

good morning, everyone. I'm happy to attend the second virtual meeting of our AMAC. Thanks as always to Ed for his excellent leadership, to the Commission staff for your hard work in preparing for this meeting and to all of you on the committee for sharing your valuable time in what I'm sure will be your thoughtful questions and commentary. The committee spent its first six months exploring a variety of timely topics.

I'm happy to see the committee now turning back to focus more on some of these same topics, retail access to private market investments, ESG, diversity and inclusion in the asset management industry and the effects of COVID-19. I look forward to the update this morning from the ESG Subcommittee. I've spoken publicly on the topic of ESG disclosure, noting my views that investors should be provided clear information about asset managers' goals and assumptions in order to understand the variety of ESG investment products that are available.

I applaud the private sector's efforts to bring clarity and consistency to this area. Such efforts will be helpful to the asset management industry as well as to the Commission whose staff reviews advisors' product disclosure and ultimately to the investors who purchase those investments.

Moving on from ESG, I also am looking forward to today's panels and would like to thank each of our moderators and panelists who bring extensive expertise in these areas. The first panel on private investment returns addresses a topic integral to the question of whether and how retail investors should be able to access the private market.

As for the second panel, I commend the committee for circling back to the topic of improving diversity and inclusion in the asset management industry. I learned from and valued the prior meeting's discussions and look forward to hearing more today, particularly from our panelists.

Finally, thank you to this committee for following up on the discussion about COVID-19. I think we and many others will spend months, if not years, studying the effects of this pandemic on our markets. I appreciate all of you pressing forward with this endeavor while our memories and data sets are fresh.

I will conclude by thanking you all again for undertaking such complex and challenging issues. I'll be actively listening to your insights and would be interested in engaging with you to glean policy ideas in all of these areas. Thank you again, and I hope you also have a great rest of the day.

MR. BERNARD: Thank you very much, Commissioner Roisman.

Commissioner Crenshaw?

COMMISSIONER CRENSHAW: Good morning and thank you, Ed. And thank you to Chairman Clayton for the very warm welcome. It's great to be at my first Asset Management Advisory Committee Meeting. I met Ed briefly last year when I was working for Commissioner Jackson. And some of you I know from other work that I've done in the past at the Commission. For the rest of you, I look forward to meeting you perhaps in person one day.

In the meantime, thank you for your time and your thoughtfulness. And I'm eager to hear your views in the challenging areas that you are undertaking today and moving forward. Specifically today, I look forward to hearing from the ESG subcommittee. As you all know, the CFTC released the management climate risk in the U.S. financial system report last week.

Among other things, the report noted that climate change poses a major risk to the stability of the U.S. financial system and to its ability to sustain the American economy. The report also highlights how climate risk disclosures offers a variety of potential benefits to issuers, investors and society. Finally, it makes clear that if regulators, including the SEC, don't

move swiftly, risk will proliferate while investors will lack the ability to properly account for those risks in their investing decisions.

So I'm interested in hearing from you, the committee, on how the SEC should respond. I'm also looking forward to the private investment subcommittee panel. Many have suggested that private markets offer higher returns and diversification benefits that public markets do not provide. I'm interested in hearing the evidence to support this perspective. And I'm also interested in hearing whether we have sufficient data to assess this fully.

I also understand there will be a panel discussion on improving diversity and inclusion in the securities markets. Diverse perspectives in both government and the private sector are crucial. These views improve our understanding of issues and ultimately lead to better decision-making and outcomes.

To me, having diverse perspectives doesn't just mean having people with different opinions. It means having people with different experiences and different backgrounds. While we've made progress on this front, there is much more we need to do. That has been made clear in recent months as our nation is grappling with how to address structural racism and

fighting a pandemic that is perpetuating income and wealth inequality. I'm interested in hearing from you on how the SEC can help the industry move forward. It's great to be here. I look forward to the discussions and thank you again.

MR. BERNARD: Thank you, Commissioner Crenshaw and all commissioners. We're grateful for your attendance and for your remarks. And now I'll turn to the director of investment management, Dalia Blass, who I think would like to share a few thoughts as well.

MS. BLASS: Thank you, Ed. Good morning and welcome to this morning's meeting of the Asset Management Advisory Committee. Before we get started, let me remind you that I'm speaking today only for myself and not for the Commission, the commissioners or my colleagues on the staff. First, I would like to thank the chairman and commissioners for your participation today. In particular, I would like to extend a warm welcome to our new commissioner, Caroline Crenshaw.

Commissioner Crenshaw has a wealth of experience at the Commission addressing issues related to asset managers. And I really look forward to hearing her views on the many important issues the AMAC is considering. I would also like to add my thanks to Ed

Bernard for his leadership and all of the subcommittee leaders, committee members and panelists for their contributions.

I appreciate the tremendous amount of work and engagement that each of you has provided to move the committee's discussions forward, particularly during these unprecedented times as we juggle professional and personal commitments in telework postures. According to today's agenda, the AMAC is considering discussions about several important topics. The first two panels will provide updates on the work of the ESG subcommittee and the private investment subcommittee.

In the afternoon, we will hear from a panel of market participants and their views on improving diversity and inclusion in the asset management industry. We will close with a follow-up discussion about the market impact of COVID-19, particularly on exchange-traded funds and operations.

Ed, before I turn it back to you, I would like to thank Christian Broadbent, Sirimal Mukerjee, Angela Mokodean and other division staff who have worked truly tirelessly to support the committee and the subcommittee's works. I also would like to thank the division's Managing Executive Office and the Commission's Office of Information Technology for yet again enabling us to meet virtually today. With that, Ed, I turn it back to you. And I look forward to this morning's discussions.

MR. BERNARD: Great. Thank you very much. So one quick AMAC update before I turn to today's agenda. Since our July meeting, Diversity and Inclusion in Asset Management has been formally made a subcommittee. And I'm delighted to note that AMAC Members Scott Draeger and Paul Greff have joined in this work with Gilbert Garcia, who has been leading it since the outset.

Turning to today's agenda, I'll let each panel leader introduce the session. And Director Blass just gave us a sense of what's coming. For now, I just wanted to offer a couple of observations. And I'll sort of break the sessions into two groupings, if you will.

Our first three sessions are going to -- are part of the ongoing subcommittee work, as you just heard. The ESG subcommittee will provide an update on their work seeking your input. And private investments and diversity and inclusion teams will each present panels with outside speakers to bring more insight into their work from outside voices. In all three cases, I think you'll see the efforts of each group to ensure we hear a range of viewpoints as part of our work. They are not yet at the point of making specific

recommendations.

And I hope you'll engage in those discussions in the spirit of fully exploring each respective topic. By contrast, our two shorter sessions this afternoon will be more focused on getting to recommendations growing out of our special focus on COVID-19-related issues in our May meeting.

Ryan Ludt led the exchange-traded products panel at the May meeting and agreed to continue leading that workstream. In that session, Ryan will provide a quick introduction, incorporating input he's received already from the committee and open up to any questions and comments. We'll test for support to see if we're ready to vote on a formal approval to submit those recommendations or if we believe there are revision -- any revisions.

After that, Mike Durbin will lead a discussion of issues his panel's team recommends be prioritized for possible recommendations relating to operational issues that were highlighted by the impacts of the COVID crisis. We don't plan to seek a vote on this material today. Rather, Mike's objective is to get input from the committee in order to move quickly to a draft memo recommendations for consideration. And I anticipate scheduling a very brief meeting for the committee later

this fall to consider those. At the end of the day, as become our practice, we'll seek initial reactions and input from the committee with quick remarks around the table in our now well-established lightning round.

So with that, if you'll forgive me, I'm going to refresh everyone on some quick housekeeping, and then we'll get underway. We're actually doing great on time. Please scroll around your screen and make sure you know where your audio and video buttons are as well as how to access the chat function. And remember to send chat functions privately to the individual you intend.

And speaking of that, if you run into technical problems, please send a private chat to Gabe Collins or Veronica Davis, who will be available for the duration of today's meeting. We'll each manage our own status. So when you're not speaking, please ensure you're muted. And when you're ready to speak, don't forget to unmute. We've all been doing this quite a bit in the last few months.

My hope is you'll keep your video on so we have a sense of our collective presence unless you're interrupted or need to step away from your screen. We will identify question-and-answer breaks as we proceed. In past meetings, it seems to work fine for folks to simply unmute and speak to raise comments or questions

or raise your hand the old-fashioned way so we -- in an analog fashion so we can see it.

Since an SEC tech support professional is the host, others can't see if you use the raise hand flag in the Webex functionality. So with that, I'll take a pause to see if I see any hands raised. Let me go to tile view. I don't see any evidence of questions.

So Michelle, thanks again for your leadership, and I'll turn it over to you for our first discussion.

UPDATE FROM THE ESG SUBCOMMITTEE

MS. BECK: Thank you so much, Ed. And let me share this -- the materials we prepared. Hopefully that's coming up on the screen. One second. Of course I'm getting a little bit of freezing going on so just a moment. Here we go. Are you able to see my screen?

MR. BERNARD: Yes.

MS. BECK: Terrific. Well, thank you, everybody. So we are back to update you on our progress since the last time we met. So let me take us to the first page. So you may recall we had five workstreams of the different folks that will be speaking today, we'll be speaking to. So we have Aye So, Jane Carten, Jeff Ptak. And Rich Hall had been in touch earlier this morning. I'm not seeing him on the screen right now. So we may not have him in attendance. Rich, if you are, please do speak up. And if not, we'll just be -- we'll lightly cover his materials because he did some very thoughtful materials. So those are the five that we're going to update you on.

For three of them, we're going to explore a range of potential actions. And I want to explain that a little bit more. So we'll have some things on the page that are not our recommendations. And it's a little bit of a risky thing to do to put that on a -- to put some of these items on a page that may not actually be things that we plan to recommend to this committee.

We wanted it to stimulate discussion and to get more information from you as a committee because seeing those on the page, we can, you know, take the pulse of the room, and folks can give us more information. Some of the great feedback you gave us after the last committee meeting gave us some direction on some of those items. But I just want to pause and make sure that nobody listening thinks that they're on the page because we are recommending them. It's not the case. We just want to explore the pros and cons of them with this group before making our final recommendations in December.

So the five work streams that we have split out in a couple ways. You know, we put up at the top

there values versus value. Is ESG -- and also, by the way, not just environmental, social and governance funds but also sustainable funds and the impact funds. We are addressing the whole cohort.

Is it about values, or is it about value? In the last meeting, Commissioner Lee pointed out it doesn't have to be an either/or. And that's absolutely the case. So you'll see that we can approach them as an "and." You can -- there are investors that are going to want to make sure that these funds are delivering according to their values, and there are investors that are going to be wanting to ensure that they deliver according to value.

And so I note that some of our workstreams fall under one category more than the other. So we'll be talking about ESG ratings and truth in labeling in funds. And that really can help underscore whether or not the contents of the fund deliver what the investor expects, which is a little bit more along the lines of values. We'll be exploring should there be any action taken about proxy voting in funds to ensure, again, that they are voting according to their values. On the right-hand side, we'll be exploring performance measurement as a way of truly getting at is the fund actually providing value as expected or as described.

And finally, at the bottom, we have issuer disclosures.

So disclosure by the issue is the securities that are purchased by these funds. It helps to support both pieces of the equation to give the truth in labeling piece of are the actions being taken that are consistent with whatever values the investor has in the fund and also to help measure whether or not they're contributing appropriately to performance.

So that was how we saw the workstream as fitting together. So I mentioned earlier we explore a spectrum of potential recommendations, everything from do absolutely nothing to extreme intervention. And again, please don't take these as recommendations. We're just exploring the pros and cons. They are straw men to gather your feedback.

And December is when we plan to come back with actual recommendations. Only three of the workstreams really required this approach because -- and they're the ones that we plan to continue to coming back -- come back to within December. So the first workstream was the one that explores values versus value. And Rich Hall has done some very thoughtful materials here. So again, I'm just going to do a callout for Rich. Have you been able to join the call yet? If not, I'll wavetop his materials. And then we'll move on to the

next section on performance. So firstly, Rich considered how ESG should be traded within the context of the Names Rule. We know that the Commission already received commentary on this topic. So we weren't planning to do much more with it.

But he -- he did some thoughtful content about the approach that he thought should be used for the Names Rule. If ESG is mostly about values, you want to make sure that disclosure is the topic of discussion, making sure disclosure features the ability to express those values. And ESG's value, it's about financial metrics and how should performance be disclosed and managed. So I'll pause there.

It sounds like we have some noise on the line. Okay. So I'll move past the Names Rule content, rather than taking the time on that. We also have an appendix in which Rich put together some answers for some of the specific questions asked earlier in the year by the SEC about how the Names Rule should treat ESG funds.

I'll just note that the disclosure questions that Rich raises are something that will come up a little bit later in the presentation as well. So the thought process here is how should you avoid being deceptive. If the investor is trying to make sure fund expresses its values. So the -- we'll pick up the disclosure item in -- under the rating systems slides in just a few more.

With the financial metrics, this is the topic we're going to be turning next to with Aye Soe. So if ESG factors lead to superior financial returns, how would you show it? And, you know, which are the different styles of investment, and how easy are they to elaborate on the performance of? So with -- I'm going to move next to Aye Soe. So Aye, I'm going to take you to the slides on performance so you can build on that last slide.

MS. SOE: Thank you, Michelle. And I really want to thank Michelle and Ed, also the division staff for really helping the discussion topics, you know, helping us guide in our thinking process and providing helpful material. So in terms of performance measurement, you know, this subsection is to think through what are the risk and returns drivers of ESG funds or ESG strategies. And what is the best way to measure whether the strategies, the financial outcomes of the strategies are aligning with the fund's objectives? So really overlaps a bit heavily with the prior sections of values versus value or values and value.

Since the meeting in May, we got a lot of very

good feedback. So our efforts have been, you know -- and our efforts have been on understanding the research that are coming out at a rapid pace on ESG strategies and the performance. And in particular, we aim to understand two things. Once is the performance of ESG strategies during COVID-19 crisis. And the second is the impact of ESG individually and also collectively on portfolio returns and risk.

And I remember Chairman Clayton mentioning that in a previous -- in our May session, you know. It's unclear as to how ESG are affecting portfolio returns individually, and collectively do they make sense, the combining. So we really want to dive deeper into that. And I bring up the -- we bring up the performance of ESG strategies during COVID-19 crisis because, as we all understand, since March, the performance of ESG funds have been much better than the broad market. There has been a lot of, you know, literature or not literature but in financial media articles even calling -- as far as calling ESG a equity vaccine.

And needless to say, you know, because of the performance, flows have followed. So ESG has been possibly the one investment style that has gathered the most assets in the last six months. So it's something

for us to understand. What is driving the performance of ESG funds during COVID-19 crisis?

So moving on to the next page, there is a lot of -- as I mentioned earlier, there is a lot of literature that's come out about ESG funds and the performance. But I want to really highlight, Michelle, the previous page. Yeah. But I want to highlight one research because it touches upon ESG performance during COVID-19 crisis. As I mentioned, COVID-19 selloff, you know, the ESG funds were better than the broad market index. As such, you know, there were claims that companies with high ESG scores were immunized against the pandemic.

There is an academic paper that came out just a few weeks ago by a group of academics from University of Waterloo as well as NYU. So it's a consortium of academics that look at the performance of ESG funds specifically. And they control for variables such as industry. That's very important because we saw energy declining substantially but tech, you know, appreciating at a rapid pace so controlling for variables such as industry, liquidity, accounting managers and intangible assets. What they found was that ESG is not significantly associated with market returns during the COVID-19 crisis.

However, what ESG returns -- I'm sorry -- the COVID-19 crisis returns are positively associated, companies, those with intangible assets, companies with heavy R&D, heavy tech presence. You know, they were richly rewarded in the last six months. That's not surprising. I was just reading last night. When you look at Apple -- and its market capitalization is larger than the FTSE 100.

And so, you know, companies with huge intangible assets are richly rewarded in the last six months of COVID-19 crisis. Innovation-related assets -- so companies with innovation-related assets, rather than those that are spending on social capital, they would -- they perform better than, you know, companies that don't during this COVID-19-related market drawdown.

So what the article is drawing attention to is oftentimes, you know, is it high ESG companies that are doing well during COVID-19 crisis or companies that happen to have high ESG scores but they -- instead -- but they are also investing heavily in intangible assets and R&D spending and innovation-driven are the ones that are doing better during the COVID-19 crisis. So I -- we bring that up as something that, during the workstream, we are heavily talking through this sort of correlation versus causation issues.

Moving onto the next slide, we also -- the workstream wanted to understand, you know, does bundling of ESG together make sense at all, and how do they affect securities' performance as well as on the portfolio level. How do they drive the risk and return. To that point, I bring up the research published by MSCI on how they -- on deconstructing ESG rating performance and how do they impact portfolio return over various time horizon.

And we want to understand, you know, should they be combined differently. And most importantly, is the sum of the parts greater than the whole or vice versa? To that sense, you know, the research split the companies with high ESG scores and grouped them, companies with ESG scores into high ESG score and then the low ESG scores. And they find that companies with high ESG score and high ESG scores outperform those with lower ESG scores.

The one thing I'd like to point out is that, you know, highest ranked ESG -- high ESG-ranked portfolio outperform more than high G-ranked portfolio, which, in turn, outperform high S-ranked portfolio, which, in turn, outperform high E-ranked portfolio.

So there is an order to which, you know, these performance are taking place. So what the research

points out is that the whole can be greater than the sum of the parts. But you can see ESG is a topic in which we have conflicting research views. Even among ourselves, we can have different viewpoints because it's an emerging topic with, you know, differing point of view that provides a rich area for debate.

Moving on to the next slide, I hope to -- oh, I'd like -- I'm having a bit of a background, yes, if we can mute. Thank you. So this is the topic that, you know, our sub-workstream spent quite a bit of time debating and talking and going back and forth, looking at -- we pointed out those two differing research because in a field such as ESG, you can have opposing point of view when it comes to performance of ESG.

So we talk at length about should ESG funds require additional performance disclosure. When we think about traditional investment style such as growth and value, you know, or a manager or fund that is in large-cap value, to catch a style drift such as, you know, if you are in mid-cap and you are buying -- securities, there are commercially-available third-party returns-based as well as holdings-based performance attribution systems that can decompose the sources of return and see what bets the fund is taking. That's mentioned earlier in a prior panel about values versus

values to see if they are being aligned or not.

And we can see those -- we can decompose the sources of return and see what kind of bets from securities selection to allocation decisions. However, ESG does not have such attribution system for investors to clearly see and provide transparency into, you know, whether the performance is really driving from ESG or not.

If you -- we look at a survey by Moody's, which shows that 71 percent of portfolio managers are unable to view performance attribution of ESG factors. Only 15 percent have visibility of ESG factors. And then another additional 15 percent say they can view ESG factors but on limited basis.

So in order for end investors to clearly understand investment outcomes from ESG investing, there is a need for performance attribution mechanism. You know, for example, understanding do the returns come from E if this is a climate change fund or if it's an overall ESG fund, do returns come from ESG altogether. At the moment, we don't have such system in the market. I like to point that out. So as Michelle alluded to earlier, you know, we are exploring this framework of do nothing and then to strong intervention model.

But in order for this performance measurement

sub-workstream to start at -- what that entails, we look at the existing SEC performance disclosure, our requirement for register funds as the baseline. We look at the -- what are the requirements for investment objectives and goals. We look at risk return summary, you know, the requirements on, you know, disclaimer as to how the fund intends to achieve its investment objectives, narrative risk disclosure, risk return -- the requirement to benchmark against broad market index. So we use that as our starting point to form our discussion.

Moving on to the next slide, so this is the -- this is the framework, the overarching framework and of which we are basing our -- we will be basing our recommendations in December from. So -- and to do nothing, which is, you know, little or no change to existing disclosure, which is in line with the current requirement for SEC performance reporting. There are pros and cons, as always; right?

On the pros side, it's low-cost for managers. There is no additional due burden. ESG is treated in the same vein as other investment strategies. And that could allow for innovation to take place in what is a nascent field. So those are positives.

However, on the difficult side, again, it comes down to providing transparency to the end investor. How do they assess performance impact of ESG objectives? And, you know -- and a do-nothing framework at the moment, that's not a -- that's not possible.

As we move away from do-nothing, we get to moderate intervention. That is to provide best practice guidelines -- description of ESG performance objectives and how that, you know, impacts, you know, the actual fund performance. This is not mandated but it's providing best practice guideline that -- the benefit of that is there is potential for greater transparency in value versus values, aligning that framework. However, there -- the disadvantage of this model is that unless mandated, compliance is voluntary.

So you run the risk of a lot of the funds not adhering to that. And if it's -- you know, and also there is a lack of comparability if you just impose it only on the ESG funds. Moving a bit further on the moderate intervention, the second part, is to best practice guidelines as well as mandate the use of secondary style adjusted benchmark. So it will be a broad market index as well as a ESG-style benchmark. That could -- that will provide greater transparency on value versus values, provide greater accountability and comparability across all the ESG funds.

Again, unless mandated, in this case, compliance is voluntary. And having a secondary benchmark is quite burdensome for fund managers. And, you know, so that increased burden is always something that we're mindful of when we're discussing through this. And at the end of the extreme spectrum, of course, is strong intervention, which is to mandate the performance attribution of ESG as well as ESG factors such -- that will provide absolute transparency in terms of, you know, understanding the value versus values.

However, it's a -- it's possibly a -- something that the market probably is not ready for at the moment. There is no consistent methodology, data system infrastructure to do so. And it's significant burden on ESG funds and may reduce incentives to develop new strategies. So with that, this is the progress that this sub-stream has done so far so -- and I'll leave it back to Michelle. Thank you.

MS. BECK: Thank you. And I expect there will be questions coming up from the committee. And we will be leaving 10 minutes at the end for questions. But if you really just can't help yourself and have a question that you need to shoot to us right now, please go ahead. If not, I was going to take us next to the proxy voting question and turn it over to Jane Carten. And Jane, you

may need to unmute.

We'll give it a moment because she may be having some technical difficulties there. I have seen her on the line. And also, we've been joined by Rich Hall, and so he'll be bringing us up at the end of the presentation to take us through some of his materials.

I'll move on to the next piece and then come back to proxy, Jane, and see if you're able to reach out to Nick Bain to see what the AV issue is. So this workstream was meant to provide recommendations for how or whether to use third-party ESG rating systems.

What we realized as we were going through this, that it was a broader question that we were asking, which is really how do you address truth in labeling concerns for ESG or sustainable or impact funds and avoid this concept of greenwashing where people might put the name on their fund but not really undertake the practices that are expected by investors. So one of the questions we asked was do you -- would third-party ESG rating systems make a difference in that. But as we looked at this broader question, some of the answers might not be about ESG rating systems but might be about disclosure. So we considered a few alternatives, again, along the lines of a spectrum so reminding you that with little or no change to the

current disclosure requirements for ESG funds has some positives. It's definitely less expensive for managers. It allows this burgeoning area to continue to flourish and create new developments.

And other funds out in the world that are not ESG funds do not always have to provide empirical proof for every claim they make that they might have a more seasoned or knowledgeable manager that's more insightful. So there are claims out there that don't need to be proven why these. And the con, however, is there is potential for misrepresentation to investors, that there might be ESG in the name but no ESG in the game.

And it's difficult to distinguish between strategies of varying quality in terms of how well they're executing on their mandate. It doesn't really provide an incentive for folks to raise the bar either. So then we looked midway through the spectrum at possible moderate intervention. And so this would be best practice guidelines related to disclosure. And so likely we'd be asking folks to explain in their disclosure as a best practice guideline how do they accomplish their ESG objectives.

We also thought that the newly-recommended taxonomy from the ICI, the Investment Company's

Institute, could be very helpful here. So they -- they've got a -- you know, do you include? Do you exclude? Do you do a bit of both? Are you quantitative? Are you qualitative? So if we, in best practice guidelines, gave an idea of what language people could center on so it would be comparable, that form of language, we thought, was actually a good starting point.

So enhancing disclosure on a voluntary basis is definitely relatively low-cost for managers. It does allow better comparability and consistency than the current state. It allows the field to continue to develop in new ways and allows for a variety of styles and doesn't lock into one particular style.

But the voluntary nature might mean that funds still represent -- misrepresent what they're doing. And, you know, you get selective disclosure. And without mandated definitions, the comparability might be misleading. So then we go all the way to the end of the spectrum, again, not a recommendation. Just exploring this topic.

What if we required funds claiming ESG to have a higher ESG score than their benchmark from a third party rating agency? And I put that as NSR -- NRSRO to make it comparable to the credit ratings. So these

would be ratings of ESG content. And it would be a consistent and measurable approach. It would derive - drive the definite kind of consistency and reliability from investors.

It would be quicker to put in place than some of the other ideas we've also had about a more thorough go in disclosure of all the -- for all the issuers that are securities in the portfolio. So I'll pause there for a moment. Jeff Ptak will be picking up issuer disclosure. But the greater issuer disclosure is, the better the investor in an ESG fund could make their own score. They could, themselves, figure out the content of the fund. The stronger the disclosure is for the underlying securities. But it's certainly not fast to get full issuer disclosure in place. So it's quicker to put into place than that.

And the cons we have, it could drive cost for -- higher. And then if you have a very small number of these rating agencies, it's going to limit development of the field. It's going to have a very particular lens on these funds and -- but if you have too many with many, many different styles, suddenly it becomes less meaningful. And it isn't really that great of an advance over the options to the left.

And finally, we note that the rating

approaches used by some of the vendors in the field currently differ markedly. They are very different styles and answering very different questions. So to bless one or the other of them would be to lock into a particular style when, like other forms of research, investors might prefer something different. So a little bit of a drilldown on this ICI taxonomy that I mentioned before.

You know, the -- if we had a -- in the option that we just explored where you have voluntary type of disclosure enhancement, you would -- we'd be asking the funds to say how do they achieve their ESG strategy and particularly to use language around do they exclude securities, include securities or use a combined approach and whether their method is purely qualitative, whether it's quantitative and uses some kind of a scoring system, or whether it's some combination of both.

Some of our discussion was that having a fund board approve that kind of disclosure might add extra quality control and extra rigor. And the ideal is to have statements about performance in shareholder reporting that attribute, in some way, to the investment process that's been laid out in the disclosure.

On the right is just a note about the

comparability of ESG rating entities. And the point of the chart is two different companies might rate the same security quite differently. So you'll see there is, you know, the range of whether one's good or bad under one rating company versus another varies quite a lot. And there is not a linear relationship between them. So those were my comments on ESG rating systems and the truth in labeling or disclosure. I'm going to pass back to see if Jane's audio is working. Well, it doesn't appear to be. I hear a sound.

MR. BAIN: Michelle, stand by. We're still having trouble, issues with her audio.

MS. BECK: Okay. What we'll do, then, is move on to the next thing that Jeff Ptak leads. And since we started the conversation, Rich Hall has been able to join so can take us home with the value versus values topic at the end. So let me move to Jeff and talk about disclosure by issuers.

MR. PTAK: Thanks, Michelle. Good morning, everybody. Thanks for the opportunity to speak on my workstream, which is opportunities to improve the quality of ESG disclosure by issuers. And we had previewed the objective of this workstream I think a meeting or two ago.

But simply put, the objective is to make recommendations to the Commission concerning guidance it should or could give corporate issuers or regulation it could act for how those issuers disclose and present ESG data and related information. Implicit in this work is the concept of materiality. Essentially, what we're saying here is that ESG issues are material. Therefore, issuers should be able to obtain the information from issuers. And that information should be comprehensive, meaningful and comparable.

And so in the next slide, we'll explore each one of those three dimensions. Thanks, Michelle. So when we think about the opportunity to improve the quality of ESG disclosure, there are those three dimensions I mentioned before, comprehensiveness, meaningfulness and comparability. So let's sort of dive into each one of those and, you know, what sort of standard might be enshrined to uphold best practices in each one of those areas.

So let's start with comprehensiveness. You could require disclosures and metrics that cover all material ESG issues. So again, that concept of materiality is front and center here. But when we're going through and assessing the comprehensiveness of ESG disclosures from issuers, then we -- we have to ask ourselves whether all of the material ESG issues have

been adequately disclosed in documents that those issuers are filing. Meaningfulness. So require disclosures and metrics that convey an issuer's exposure to each material ESG issue that's been identified in standards that acknowledge the dynamic nature of materiality.

You know, we have to acknowledge that materiality can change given the state of a business or other circumstances that surround a particular issuer's business. And so that should be reflected in sort of the dynamic nature of the way issuers are defining materiality and the information that they are conveying to users of their documents, investors.

Comparability. Required disclosures and metrics need to balance standardization to promote comparison across industries with adequate specificity to enhance comparability within industry. So that's the third of the three dimensions, again, to make this a bit more tangible and to form some organizing principles for how one might define their approach to enhancing the quality of ESG disclosure.

Why don't we go ahead and we'll jump another slide here? And we're going to examine each one of these three dimensions and then some of the issues that I think investors have been confronted with, you know,

in the absence of a standard for comprehensiveness, meaningfulness and comparability. And we are giving you a few examples. This is an exhaustive list.

But when we think about the comprehensiveness, I would say that one of the real practical issues that investors are facing when they're trying to get information on -- ESG issues is that not every public company is disclosing ESG risk. And that's even less so for private companies.

With respect to fixed income, disclosure can be poor. And it can be issuer or lender-focused but not both. And so it may not be stakeholder-universal in the way the information is being presented. Again, that has a bearing on the comprehensiveness of ESG disclosure that's provided by issuers of those securities. Let's turn to meaningfulness.

One sort of important kind of point of orientation is whether the disclosure, the information that's provided, is backward-looking or forward-looking. I think that what we find is that, you know, there tends to be a focus on backward-looking, more retrospective type of disclosure versus forward-looking disclosure, which can be quite valuable in its own right.

There can be voluminous metrics. But that can challenge analysis. It's the kitchen sink approach. Or

it can make it difficult for investors to really home in on what are the most material ESG issues that could have a bearing on that issuer, therefore, the investor's experience with that instrument.

A lack of positive impact data. You might get plenty of information on what it is a firm, an issuer, is doing to mitigate negative impact, negative consequences, less so about forward-looking positive impact data. And then there is cherry-picking. You know, oftentimes what investors will get -- I don't want to say oftentimes. But too often what investors will get is something that's more like a marketing -- than a truly meaningful document that's at the level of the disclosure that we've been accustomed to receiving from issuers that's more financially-oriented.

Let's turn to comparability, which is the third of our three dimensions. And there is no shortage of standard setters and different stakeholders that are part of the process, all approaching this in a very circumspect, studious way and putting their best foot forward. But it does create challenges for investors insofar as issuers are responding to multiple frameworks and trying to reconcile between them. And so that can detract a bit from comparability when, say, investors are trying to compare one issuer to the next. Why don't we go ahead and we'll jump to the next slide?

Thanks, Michelle. So now we're going to talk about gaps in disclosure and the role regulation can play. And I would preface this by saying I think it's consistent with some of the comments that you've heard from our other subcommittee members and Michelle, you know, really sort of the way to receive this. This is information about potential direction of travel, of recommendations that we might make in this particular area.

And when we thought a bit about where the gaps in the disclosure are and the role regulation could play, it really coalesces in a few areas, standard setting, disclosure framework, standardization and presentation. And so we have slides for each one of these. And I won't belabor any one of them, just in the interest of time.

But why don't we jump to the first one, which is standard-setting. In here, there are various choices that -- that one would have as far as how do we go out and promulgate a set of standards that guide the way issuers provide information through disclosure to investors? One of the choices that you can make is to embrace third-party standard-setting organizations, ESG reporting metrics. You could make third-party standard

setters recommendations authoritative and binding. There is precedent for this, as we well know, when it comes to financial disclosure. That's GAAP.

You can also hold third-party standard setters accountable for harmonizing existing standards. Again, there is a lot of thoughtful, very dogged work that's being done in this area. The challenge can become making sure that it works in harmony and so setting up a process or a framework by which harmonization takes place. This is a valuable role that standard setters can play in helping to ensure that disclosure information is as meaningful as possible and then, of course, encouraging collaboration among standard setters, which is probably the best way of all to ensure that there is uniformity in the way the different standard setters are approaching this area.

Let's move to the next area, which is the disclosure framework, again. There are different choices that -- you know, that one faces, rules-based versus principles-based. What one could do is require a principles-based disclosure framework that focuses on material issue, you know, and establish a balanced approach to required disclosure, you know, sort of think of it as core and explore. There is a focused list of mandatory disclosures that are applicable to most

issuers. They have a certain universality. And then you supplement that with specific disclosures that are tailored to the business or the industry concerned. It seems like that sort of balanced approach could satisfy multiple stakeholder groups and also boasts consistency insofar as the core travels from one industry to the next.

And then expand reporting requirements from the largest firms to nearly all companies. Though we do acknowledge that given the burdens, you know, and the fact that some firms are better-equipped than others to respond to different disclosure requirement frameworks, it could make sense to adopt a multi-tier approach that's adapted to smaller issuers who, again, may not be resourced to provide disclosure and other metrics at the same level as larger, better-resourced firms.

Let's turn to the third issue, standardization. And so when we talk about standardizing, we're talking about industry-specific disclosures and environmental impacts, starting with climate change, forward-looking disclosures, backward looking measures, discussions of risk management and climate scenario analysis and then what we're thinking of as baseline ESG disclosures.

But really what you want to make sure is that,

you know, you have sort of like the more important themes and categories consistent from issuer to issuer. And there are certain baseline metrics that are contained within the disclosures that facilitate in comparison across issuers. Let's turn to the fourth area. And that's presentation. And the notion here is that you make ESG disclosures look like other financial disclosures. What are some examples of that? The notion is that the data should be temporally aligned with financial disclosures.

You should encourage integrated reporting. A single encompassing report, like an annual report, and it is machine-readable in a standard format with standard taxonomy. So in many ways, it becomes interchangeable with a financial disclosure that is well-established and that all of us are very familiar with.

Let's go ahead, and we will jump to the next slide. And so this slide is probably familiar to you by now. You know, do nothing and strong intervention, they really bookend the potential recommendations that we could make for this workstream in our review, each of these. One reference point that I would remind everybody of and this is something that I might have mentioned when I reported out previously the Investor as Owner Subcommittee of the SEC Investor Advisory Committee presented a set of recommendations to the SEC in May of this year. And so I would say that some of the choices, the options that we are presenting here are congruent with what you would have seen from the Investor as Owner Subcommittee in that May 14, 2020 document. But I will go through each one of these briefly so that you get a sense of what the potential directions of travel could be depending on whether you chose to do nothing, to moderately intervene, or to intervene more heavily.

So let's start with do nothing. And that is largely status quo. You make minimal changes to the current issue or disclosure requirements. The pros, the benefits of that are there is obviously a low cost and burden for issuers. It does facilitate a market-driven response, where investors come to reward issuers who uphold best-disclosure practices, and it encourages others to follow those practices in the belief that they, too, will be rewarded in the future.

What are the tradeoffs, the cons? It doesn't uphold best practices for comprehensive meaningful comparable disclosure in the various ways we have described. And it can impede development of a common disclosure standard and framework, which results in

continued inefficiency. We are kind of just all over the place. And you have issuers that are responding to multiple frameworks and standards, and it is difficult for them to be as efficient as they would want to be.

Let's move over a column to "Moderate Intervention." Under this approach and there is a lot of different sort of do-nothing, moderate, strong intervention approaches that one can take. In this, you are encouraging and then you are mandating disclosure per principles developed by third party standard setters. And you are curing by materiality and issuer size.

What are the benefits of this approach? It gives issuers some time to prepare for and adapt to emerging disclosure frameworks. It taps a successful model, Generally Accepted Accounting Principles, promotes a common disclosure standard without being overly prescriptive, and differentiates per materiality and issuer size. So there is a certain amount of tailoring and customization that you can do, acknowledging that there is not the same state of writing this across issuers as perhaps there would be when it comes to financial disclosure that we are accustomed to.

What are the cons? Industry and regulators

haven't coalesced around a third-party framework yet. And it is a gradual patchwork approach, which might not approach standardization and comparability in ways that benefits users of disclosure.

Finally, I will talk about strong intervention, which is the right-most column. Under this approach, you are codifying a comprehensive set of disclosure rules through regulations and really irrespective of materiality and issuer size. So, basically, what you are saying is that there is one standard. It is rules-driven. And it applies to every issuer.

What are the benefits of this? It certainly doesn't suffer from ambiguity. It entrenches a clear, comprehensive standard for disclosing ESG matters. It also boasts authoritativeness, consistency, and obviates the need for a patchwork approach that could take time to implement and, arguably, courts the risk of confusion.

What are the cons, the tradeoffs? It fails to acknowledge differences, any ESG issue materiality, issuer size, and readiness. It puts a potentially heavy burden on issuers to implement disclosure, and a rules-based approach could detract from disclosure meaningfulness insofar as it devolves into a set of

boilerplate disclosures that may or may not be pertinent to the issuer concerned or simply not be useful to an investor that is trying to get a sense of what the future could look like in terms of risks that would be bearing down in that particular issue from an ESG standpoint.

So, hopefully, that gives you a picture of what the different directions of travel could look like under a do-nothing, moderate intervention, and strong intervention approach. And, with that, I will go ahead and turn things back to Michelle.

MS. BECK: Terrific. So we apparently solved all of our technical issues, and we are going to be hearing first from Jane on the proxy-building issue. So let me take us back to that slide. And then we will finish it off with Rich, who won't appear on video but will be here on audio.

So, Jane, are you able to address the proxy voting?

MS. CARTEN: Good morning. Can you hear me?

MS. BECK: Yes.

MS. CARTEN: Great. Awesome. So that was a lot of traumatic buildup with technical issues to not much of a slide because when we were considering what requirements should given ESG planned proxy-voting practices, one of the things that became quite clear is that the SEC had just voted to amend rules concerning proxy solicitations and had provided supplemental guidance just recently. And we definitely took seriously the idea that it is okay sometimes to say doing nothing is, in fact, what should be done at the moment. And in the end, because of the recent amended rules, we decided that additional conditions don't need to be placed on proxy voting at the moment, that some of the benefits to the amended rules that the SEC put forward included additional conditions to the availability of certain existing exemptions for the information and filing requirements of the Federal proxy rules that are commonly used by proxy-voting advice businesses and disclosure of conflicts of interest between proxy adviser and affiliates, clarity that proxy-voting advice generally constitutes a solicitation, and failure to disclose certain information may be subject to any provisions of the proxy rules.

So we believe that these actions effectively improved investors' ethical outcomes and in combination with Rule 13(f) do provide an adequate level of transparency with respect to proxy voting, whether a fund is designed to include ESG considerations or not.

MS. BECK: Excellent. Thank you so much, Jane.

So we don't plan to move forward with any recommendations in December on this. I am now going to take us to the value of risk slides. So Rich hopefully will be able to address these items now. Rich, are you on the line?

MR. HALL: Yes, I am. Can you hear me?

MS. BECK: Yes, we can. Thank you.

MR. HALL: So we were asked to consider three questions as part of this workstream. One is, how should ESG be treated within the context of the name rule? And that really changes upon an issuer determination of whether you are using it as a strategy or whether you think it is a fundamental issue.

And then to go into a dissection of, well, values are about investor choice. And is there any difference? If it is about a choice, how should that possibly impact disclosure versus value? And that is maybe a manager or a company is claiming that their ESG performance enhances their opportunity to create value for the investors. And if that is the case or that is the assertion, how should that change disclosure?

So maybe we can go to the next slide, please. So just a quick recap of the names rule for those who

haven't studied it. The names rule has been in place for a significant period of time. They put it in, the SEC put it in, place because they wanted to make sure that investors may rely on a name, in part, in terms of deciding on whether or not to make an investment in a fund. And they wanted to make sure that the fund names were not misleading and that there was consistency between what the fund name asserted it would do or the assets that it would invest in and what actually we found under the hood when we looked inside the investment holdings.

And so the percentage has varied over time, but presently if you fall within certain names category requirements, 80 percent of your assets by value need to line up with what you are asserting in your name. And so what are those things that require that alignment? It is an interesting mix because on the surface level, it is pretty obvious things like the type of investment are you investing, it is a stock fund, it is a bond or the industry of investment, and then also some regional categories, so either by a broader geographic region or country.

But what is not included are things that would seem to be something that investors would consider in a name. That could be the investment objective, things

like low volatility or capital appreciation. And then you get to the point where it probably intersects, this conversation intersects, most is strategy, ESG strategy, or should strategy by the name. And strategies today are excluded, their growth, value, ESG, low-carbon. These are all things that would not require any fund manager to have alignment between the name and the underlying assets.

The protections about not having materially deceptive or misleading names still do apply. So if we can go to the next page, now we will kind of get into the consideration of the first question. So how should ESG be treated under the names rule? So right now, as I just mentioned, ESG is considered a strategy. So it does have the basic protections that there can't be blatant greenwashing, throwing the ESG in the name, when there is no intention whatsoever to incorporate that in strategies. But it is important to really think about what are the attributes that are being used in the selection process. And then that dictates whether ESG is really still a strategy or does it at some point possibly become fundamental?

And I would say that it seems like on the strategy side, that that is an easier thing to assert than there is a lot more latitude about it. At some point, though, it may become fundamental. And, then, there is a determination that needs to be made about whether or not we shift it to be so fundamental that it may qualify under the other elements of the names-rule license? The easiest example I could come up with on that is that you were looking to apply either inclusion or exclusion requirements in your asset selection. And based on your criteria, maybe the inclusion is so select that you drift to the point where you are basically an industry bump. And, then, if that is the case, should there be some sort of line because you have zeroed in on such a tight definition that that comes to task?

So I think there is work to be done here to think about like where is that line and how do you tighten this up so that investors really do get what they are asking for or what is being marketed to them? And I would say, note, that I know that the SEC is seeking commentary from the market about whether strategies and ESG, in particular, should become something eventually.

So we go to the next page. I think we should be on that one. If ESG is about values, then how should that affect disclosure? So, again, you know, we continue to have basic protections under the names rule. But when you go into the zone of values, that is an

investor making a choice. Investors do have a right to make choices about how they want to invest. Especially individual investors have the opportunity to say, "I am willing to either hopefully enhance but possibly forego return by taking certain risks" that go along or are intended with a particular strategy here.

And so when you get to that point, it seems like the investor should bear some burden of diligence to confirm that they are actually getting what they want. And at the same time, you have to be able to have some means for verifying that, so a trust-but-verify type of mentality so that the disclosure is sufficient for the investor to really make an informed choice about what they are buying and if it is actually going to hopefully accomplish the choices they are making in trying to express their individual values.

And, ultimately, it seems like based on that, that the investors should shoulder that burden. And if they can't come to satisfactory resolutions in their investigations and diligence, then this is actually going to happen that they should be the ones who should say, "Well, I am just going to need to walk away because I don't have the information or the disclosure to support it." So I would encourage robust disclosure, but if in the end, if it is a value-based decision, then

the investor probably should bear a significant portion of the burden in the decision-making process.

And, then, lastly, if we go to if it is about value. And so we talked a little bit about this already. Right? Some practitioners believe that ESG factors will lead to superior returns in the long run. And there are two primary drivers that I have heard are the most common. One is that ESG risk can be material. And they may not be properly priced today. And so if you can investigate those from a fundamental perspective and have a better means of assessing them, then you may make better investment selections and drive further value for your investors. And the second is more centered around venture capital flows and that there is a significant movement in the flow of capital that is expected to happen in support of various businesses that may be social impact-related or may be more environmentally friendly and that those flows alone have the potential to drive market value. So we should try and be in position ahead of flows and, therefore, benefit by the added demand. So those are the two fundamental reasons that I have heard explain it.

We talked a little bit about inclusion and exclusion. Those two can be very strong in terms of limiting an investment universe and creating potential

risks in terms of the end holdings that a fund needs to have or will have. And so that seems like pretty strong disclosure should be required there so that investors can adequately understand the risks that they are taking relative to a broad market risk, which you well-know. Once you start taking it down that field, you begin to track and introduce different factors in investment. So an investor needs to be able to understand that so that they are making informed risk decisions.

The third part of ESG is also pretty common. And that is we use it as part of the overall investment decision-making mosaic. Right? So we have all of our basic fundamental financial metrics and other things that we use to limit the investment managers who can select the assets. And one of the things that we include in that is ESG. So that would seem not to argue for any asymmetric disclosure. Right? If ESG is a significant portion of your investment-selection strategy, then you should just be describing that to the same degree that you describe everything else that flows into your investment strategy.

And I think that all of that, really, goes to the question of managers are out there generally to make a profit. And they are seeking competitive advantage through the ways that they employ information to select assets, which hopefully generate attractive returns or more attractive returns relative to benchmarks or competitors. And, therefore, they should enjoy the opportunity to protect them sort of as part of their process.

So I think that is going to be a fine line, not to make a manager kind of talk about the secret sauce in such detail that they give away their intellectual properties. At the same time, how do you make them disclose enough of what they are doing so that investors understand the risks that they are taking when they go into it. The biggest is finding that balance when it comes to, is it about value.

I think those were the three questions that we had. There was another set of questions that the SEC did ask in its solicitation for commentary on the names rule. I will put a slide up, and we will talk about that.

MS. BECK: And, Rich, if there are more questions on that topic, we need to hear the questions.

So it is just breaking up. It sounds like somebody needs to go on mute. Okay.

I am going to wrap up on next steps. So during the question period or afterward or in some of

the notes we sent around after, we are looking for the feedback of the committee members and the reaction to the range of actions. You know, are there people who are strong components of do nothing? Do you think we missed something in the various forms of interventions of the three that we explored? And during the next quarter, we are going to be meeting with investors and issuers to drill in more on these disclosure questions of what would the burden be, what is most useful to investors, what is most difficult for issuers to provide so that as we work toward our final recommendations, we get a bit more of that external perspective when we finally come back in December.

So I am going to pause now to see if folks have questions. We have about 10 minutes for questions. Oh. Joe Savage?

MR. SAVAGE: Thank you.

First of all, that was a great presentation, really well-done and really good, Michelle, in terms of dealing with the technical difficulties. So kudos for that.

When I was watching this, you know, I think there are a lot of focus on what disclosures need to be in the prospectus or the annual report and whether it needs to be standardization of ESG factors. You know, a

lot of what retail investors see, though, they don't look at the prospectus. They don't look at the annual report. They just look at either an ad, whether it may be a print ad, a television ad, a website, and the communication tends to be you know, they try to grab the readers' attention. So it may be fairly short. You know, examples might be the Morningstar rating of a fund or if it is a fixed-income fund, the percentage of assets that are in AAA bonds.

Have you guys thought about not just how your recommendations will impact the documents that are filed with the SEC but also should there be recommendations in terms of marketing material, in terms of whether there should be some kind of standardization for the rules governing advertising? I mean, just to sort of give you an example, today if a FINRA analyst looks at fund material, they are basically going to see if it is consistent with the prospectus. So if we see an ESG fund ad, we are going to make sure that that is consistent with the prospectus for the fund, but we are not going to question whether the investments in the fund truly are meeting ESG criteria because that is just not our role.

So I just want to throw that out and see if that is something you have given thought to and whether

you have any recommendations. Thank you.

MS. BECK: Well, I will pop up first. You know, it hasn't come up much in our discussion yet. So it sounds like something we need to add to our final work to figure out where the once we decide what we are going to recommend around the official forms of disclosure, then perhaps connecting the dots to what it means for advertising would be a piece we should add as well.

It looks like a question from Russ.

MR. WERMERS: Hi, Michelle, and thanks for a great panel discussion. I just had a quick thought. I'm sorry. Can you hear me? Okay. I just had a quick thought. It looked like you had two screens where you had several frames of thought in your panel, which were great. You had two streams that kind of caught my attention, though. One was how funds should or might be compelled to have more truth in advertising I would guess as the SP funds. And the second screen Jeffrey I think discussed this was issuers, issuer-level disclosure.

I think this is I am just wondering if the panel has thought about tradeoffs between the two because the fund manager can be thought of as a monitor. Right? He monitors or policies his underlying issuers.

And so I guess maybe the SEC needs to think about, do we monitor the monitor or do we monitor the underlying agents here?

And as an example, as an example, stocks, firms, issuers can brainwash and get great MSCI scores. And the fund may look just fantastic. And, really, it has had no effect. I mean, the fund has done the best they can, but the fund investors are not getting what they think they are getting in the underlying assets.

MS. BECK: I will start. And, then, Jeff, I will probably pass it over to you. One of the discussions we had in the subcommittee is if you had a very thorough, very extreme form of issuer disclosure that covered all of the bases and had great reliability, you wouldn't need as much of the fund disclosure that we are talking about because investors could or third-party agencies could use publicly available data to rate and score and everyone could rely on it. So that is the more fundamental change that would actually address most of these other issues, but it is much harder to put in place, much harder. You know, it is the length of time, of cost, and how do you get to that level of certainty that that issuer disclosure is good. But it was the more fundamental thing to do in order to solve these other problems that we are talking about in this area.

So it was about, you know, not letting the perfect be the enemy of the good because to get to that level of perfection is pretty difficult, but it is the more powerful intervention. That was something that I think we thought as a subcommittee.

Jeff, did you have any other thoughts?

MR. PTAK: Yes. I think you sum it up well. And, Russ, you make good points there. I guess sort of the frame that I was coming at this from from my workstream, which was on issuer disclosure, is, as we know right now, the SEC plays a role, both in monitoring, if you will, investment companies and the issuers into securities they invest. And so I think that we were thinking about potential approaches to ESG disclosure in a similar way that you would need to have frameworks that are pertinent to both of those areas, recognizing their importance to investors, whether they are investing directly in an issuer securities or they are doing so with the help of a professional investor in the form of an investment company.

As far as greenwashing goes, I recognize that there is a diversity of very thoughtful views on this. As I have reflected more on it, I do tend to think that that problem begins to recede a bit as you have a set of disclosure requirements that are more comprehensive,

meaningful, and comparable just because it is going to be that much more difficult for a fund to, let's say, go through and fake it to greenwash because we are going to have a rich set of disclosures. They are going to evidence whether or not the firms they are investing in are, in fact, upholding best practices from an environmental, social, or governance standpoint; whereas, today, I don't know that we could necessarily say that. And I know that there have been different solutions that have come in and tried to compensate for some of that ambiguity, including ratings. Those can suffer from some of their own issues. So I do tend to think of issuer disclosure as something that could help to address not just some of the issues that we are seeing at the issuer disclosure level but also at the fund level with greenwashing.

MS. BECK: Thanks, Jeff.

We have got a question from Commissioner Roisman, then after that Scot Draeger. So Commissioner Roisman?

COMMISSIONER ROISMAN: I can certainly wait until Scot. I want to give the committee ample time. So I will defer to him and come back at the end if that works.

MS. BECK: Okay. All right. Scott, go ahead.

MR. DRAEGER: Hi. Out of respect for the commissioner, I will sit back and follow the commissioner. I want to make sure you indeed have the time to ask the questions.

COMMISSIONER ROISMAN: I really appreciate that, Scot.

And thank you, Michelle. I think that was a phenomenal presentation. I really commend you and the subcommittee for great work. I actually really appreciate the fact that you guys put our more than you are actually necessarily going to do, but it is a great point for getting input, not only from fellow members of the committee but also from hopefully the public will engage. And it is great that you guys are meeting with both issuers and asset managers. I just think that was really an exceptional presentation.

I just want to have a question relating to the issuer disclosure and materiality. I think I just want to give you my perspective. And I think this is where it would be helpful just as something to think about. I think we all agree that there is definitely ESG information that is material to investors. And companies have different you know, companies are just differently affected by it, but to the extent that they have ESG risks or things like that, they are required to disclose that. And so there have been portfolio management strategies such as growth and value strategies for a long, long time. And certain information might be useful for an asset manager or for each one of those, but we haven't necessarily based our issuer disclosure requirement on what is useful for a particular investing strategy. So the question I have is like, should ESG strategies necessarily be treated the same way?

To the extent that you guys are talking about ESG as a material piece of information that all asset managers need to do for all of their investment decisions, I would think that makes sense. I have heard that from many asset managers. But in terms of I think when I am approaching whether we need to have a new disclosure requirement for issuers, it is to whether that is a material piece of information for investors to make an investing decision.

And so I just want to point that out. And, you know, to the extent you are willing, I would love to follow up with the subcommittee and have a greater discussion about this and other pieces.

MS. BECK: Excellent. That would be very helpful. I know that Jeff has done a lot of thought about that materiality question. And the point is a

good one that it is not just about for the convenience of certain kinds of investors, but it needs to represent real risk or real factor driving performance.

MR. BERNARD: Michelle, this is Ed. I am going to suggest that maybe the next question be the last one.

MS. BECK: Okay. I saw that Gilbert Garcia had his hand up. So, Gilbert, go ahead.

MR. GARCIA: Thank you very much. Michelle and to all of the subcommittee members, should there be a requirement that managers that are doing these ESG funds and so forth have to have a minimum requirement of following ESG best practices of some sort themselves?

MS. BECK: In terms of their own hiring practices, their own staffing, their own

MR. GARCIA: That's right. In other words, before you can even I am just speaking out loud before you can even manage an ESG fund, if you are not ESG yourself, whether it is your board, whether it is your partners, whether it is staff or something like that, I mean, should you start there?

MS. BECK: We can take that under consideration. I don't know if any of the committee members have a response on that.

(No response.)

MS. BECK: So great. One for us to think about. So thanks for raising it. And we will bring it in.

So, Ed, if that needed to be our last question, there were still a few hands raised. And so either in the around-the-room period or afterward in email, we would love to hear your questions or your comments because it will help make the final presentation that much better.

MR. BERNARD: Yes. If I could? Unfortunately, I am the guy in charge of keeping us on time. So, first of all, that was a phenomenal panel. Thank you to all. For those who had technical difficulties, we feel your pain. We have all been there.

And, Michelle, you did an extremely deft job in navigating it. I think you have now shot to the top of my list of people I want on my team in a crisis. So congratulations to all.

And I would encourage everyone, particularly if you still have questions but there is a lot of rich material there. Go away. Read it. If you have additional thoughts, please reach out to Michelle or subcommittee members. And I suspect they will be reaching back out to the committee as well for further

input.

Before we go to break and I am going to suggest since we are a couple of minutes over, we will come back at 10:45 sharp Eastern Time, but Dalia Blass wanted to make a quick comment about a technical problem that most on the committee probably aren't even aware of. So Dalia?

MS. BLASS: Thanks. This was extremely informative and a very thoughtful presentation. I know I have a ton of questions, but I will save them.

Just for our external viewers, apologies. I know the broadcast cut off for a few minutes. One slide I think was not being covered. We apologize for that. Committee members, you probably were not aware because the WebEx was on a different platform. We are going to see an archived version of this webcast, whether we can fill that gap. So, again, apologies. And we will do our best to see if we can fill that gap.

And apologies to the subcommittee members. It was an extraordinary presentation. So sorry that one little piece of it was not out there. It truly was about like a minute and half, so not an extended period of time. And we will see if we can get a fix going. So thank you for that.

MR. BERNARD: And I would just say to those viewers if you are interested in the topic, just keep an eye on our webpage, on the sec.gov. And I am sure as and when we can fill the record, it will be there for you.

So, with that, everyone, let's take a 10-minute break. And I will start the proceedings again at 10:45 promptly. Thanks so much.

(A brief recess was taken.)

MR. BERNARD: Let's get started again. Next up is our Private Investment Subcommittee, chaired by Rama Subramaniam. After a brief update on the committee's ongoing work, this session will be devoted to a panel discussion with four distinguished speakers: two from industry and two from academia.

As I noted in my opening remarks, I think we will hear a range of views today and at times disagreements on some basic concepts, such as returns and how to measure them. As our purpose today is to focus on the issues and not any particular market participants, our speakers have generally refrained from associating with specific firms, even when that information is in the public domain. For those in the audience who are interested in more detailed information, I think you will find the footnotes and references on their slides to be helpful.

So, with that, I will turn it over to Rama to open the session.

MR. SUBRAMANIAM: Thank you.

I hope everyone can hear me. I am going to show you my screen. Wrong screen. Right. Can people see my slides?

MR. BAIN: It looks good, Rama.

MR. SUBRAMANIAM: Yes? Thank you, Ed. I want to thank the SEC commissioners and staff for the opportunity to present an update on the Private Investment Subcommittee and our work to analyze whether wider access to private investment should be recommended. I particularly want to thank Christian Broadbent, Emily Rowland, Sirimal Mukerjee, and Angela Mokodean for their help in pulling together our presentation and to Erik for moderating.

Our agenda today will be taken up by a panel discussion moderated by Erik Sirri with four eminently qualified individuals spanning academia and the industry. I want to thank Noel, Bryan, Josh, and Ludovic for sharing their valuable insights. They will focus on the first workstream the committee set themselves. That is whether private investments provide additive and/or diversifying returns to a typical public markets portfolio.

I hope to cover my slides in around 50 minutes, allowing 75 to 80 minutes for the panel. And, as such, I plan to briefly cover the following: firstly, a quick recap on why we are focused on potential expansion of access to private investments. This really is a recap on the supply and demand dynamics in U.S. asset management; secondly, an update on the two main workstreams, the analysis of whether private investments provide better and/or diversifying returns will be the focus of the panel. And I don't plan to say much more on that today. I will briefly touch on our analysis of the regulatory landscape as we start to think about recommendations and how they can be incorporated within the current regulatory landscape.

Next, I want to briefly touch on design principles. This is really an attempt to solicit feedback and comments from the AMAC Committee members after the meeting. So for now, we will just briefly discuss some of the design principles we are thinking about.

And, lastly, I will spend just a couple of minutes defining and discussing a couple of key terms that will be used on the panels just to make sure that everyone is on the same page. I apologize if people are very familiar with these terms, but given the wide

diversity and range of people on the panel, I thought it would be worth spending five minutes on that.

With that, let me start with the supply and demand dynamics in U.S. asset management. And, really, this is a recap from previous slides in discussions from other people that have presented to the committee.

First of all, on the demand side, we see the pool of investment assets continuing to grow due to demographics and macroeconomic factors. Within the asset management industry, we see retirement savings representing more than half of the AUM. And within retirement savings, we see a dynamic where IRAs and self-directed and defined-contribution plans; i.e., 401(k)'s, continue to increase in size and relative share of retirement assets. In contrast, defined-benefit plans continue to reduce. And many of these plans are transitioning to the payout phase of their cycle.

This is a slide I have used a couple of times. And I thank Michael Goldstein again from January showing the growth in the U.S. money-management industry, both in absolute terms as well as a share of GDP. The U.S. money-management industry at the end of 2019 stands at about 45 trillion in size.

Another Michael Goldstein slide from January breaks down by percentage terms the composition of those assets. Retirement assets, the bottom three bars, have grown in relative proportion, but within retirement assets, we see a growth in IRA accounts and a decline in defined-benefit pension plans.

Drilling into the retirement side just a bit more, this is a slide from the investment company Fact Book, which they graciously allowed me to use, which shows a breakdown in trillion-dollar terms of different retirement assets. The message here is that IRAs and 401(k) plans have grown from approximately $2.2 trillion in 1995 to $17.2 trillion in 2019 and have grown from 33 percent to over 53 percent of total retirement assets.

In contrast, in the same period, defined-benefit plans, whilst they have grown in absolute terms from 3.4 trillion to 10.1 trillion, as a percentage, they have fallen from 49 to 31 percent. So the clear message is that we have an increasing amount of retirement assets and within those retirement assets an increasing amount of assets that are largely self-directed and limited to public markets; whereas, the private market participants over time and plans are getting smaller in proportion and size.

What about the supply side? Here is an even clearer picture. We are seeing public equity markets

whilst larger in absolute dollar terms getting farm more concentrated with fewer listed companies and dominated by large companies. We are seeing companies staying private for longer and getting larger whilst they are private.

We are also seeing private fundraising easily surpassing public fundraising. Again some slides to highlight this. This was a slide I had in my last presentation, the yellow line showing the market cap of listed companies growing; however, the number of listed companies dropping from the peak of about 8,000 in the mid '90s to around 4,000 currently. Meanwhile, we see private companies staying private for longer. Whilst not quite at the peak of 14 years, which was around the dot-com and the financial crisis, we are seeing median age of around 10 years, as opposed to 6 years for private companies that are staying private longer.

And, lastly, we see the concentration of public companies in the S&P 500. The 2 lines show the percentage of the top 5 in 10 companies, the makeup of the &SP 500 with the top 10 companies now accounting for around one-third of the total market capitalization of the S&P 500. The bottom part of the slide slows the absolute market capitalization of the largest companies. Not only has the composition changed since 1995, when

General Electric, AT&T, Exxon, and Cola-Cola dominated the S&P 500 top 5, the top 5 companies now are all over a trillion dollars and in the case of Apple over $2 trillion. They comprise Apple, Amazon, Microsoft, Google, with Facebook coming up to the $1 trillion market. So we are seeing a far greater concentration of public companies and in some ways less choice in public markets.

Turning to private offerings versus public offerings, this is a slide from a paper from the Committee on Capital Markets Regulation. I would say that all of this material is, by the way, available at S-links at the back of this presentation.

We see that for the full years of data, 2015, '16, and '17, equity raised via IPOs is more than double the equity raised by private Reg D offerings. Similar SEC data but on a wider universe pulled from a white paper referred to at the bottom there shows Reg D offerings of over $1.8 trillion in 2017 versus registered equity.

Now, the Reg D offerings here cover both initial offerings and follow-on offerings and cover both corporate and noncorporate issuers, so a much wider range of offerings compared to the previous slide. But the trend is clearly there in that private offerings are

much larger than public offerings and within private offerings, Reg D is still by far the most widely used exemption for private offerings.

We wanted to briefly touch on the regulatory landscape. I would say our analysis on the regulatory landscape has been to date an initial survey of what are the main areas we would need to think about and either fit within or recommend changes to in order to promote wider access to private investments.

Where we have landed is there are really three areas that we need to focus on. The first is the Securities Act, which provides for various exemptions from registration for issuers of securities. Reg D is still the widest used exemption, but there has been a substantial growth in the number of exemptions available, including things like the Reg Crowdfunding for around a million dollars and the Reg A and Reg A plus offerings for higher amounts that were introduced or updates with the JOBS Act.

However, as one of the speakers said at the start of today it was Commissioner Clayton, actually we are likely to be looking at people accessing private investments through a fund structure. And, therefore, the Investment Company Act needs to be considered and, in particular, either fitting within the registered Investment Company Act framework or discussing the much higher requirements of being a qualified purchaser.

And, lastly, we briefly want to touch on the additional requirements for 401(k) under ERISA. I don't intend to spend too much time on these slides in the interest of getting through the material, but the first thing is the Securities Act, which applies to issuers. As mentioned before, there are very safe harbors in exempt offerings, but by far, the largest used exemption is the Rule 506(b) of Reg D, the so-called accredited investor and non-generally solicited offers. The accredited investor definition has two main prongs: the income, or net worth, prong requiring in come in excess of 200,000 or 300,000 in the case of joint income in each of the last 2 years or a net worth in excess of 1 million. We have seen recent extensions that the SEC has promulgated to the extent accredited investors should specify people based on professional certifications, designations, or credentials.

As mentioned, the Investment Company Act becomes important where we are talking about investments in funds which themselves invest in private companies. Most PE funds or most private funds use two exemptions: the so-called Section 3(c)(1) or 3(c)(7) exemptions.

Both are nonpublic offerings. Section 3(c)(1) limits the number of investors to 100, and Section 3(c)(7) requires qualified purchasers. Qualified purchaser requirements are primarily financial and much higher than accredited-investor requirements, generally requiring more than 5 million of investments for individuals.

The alternative is to be a registered investment company. Registered investment companies come in various flavors; are open-end, like mutual funds; closed-end; for example, interval funds; and ETFs, which can be either open-end or unit investment trusts.

There are substantial requirements and restrictions of registered investment companies which are beyond the scope we are covering today. That includes investment advisory contracts, corporate governance requirements, limitation on affiliated transactions, use of leverage, and other things.

Focusing, however, on private investments, it is important to note that open-end funds are subject to a general 15 percent threshold on acquiring illiquid investments, which makes sense given that open-ended funds have to be able to redeem on fairly short notice, normally daily, in order to provide liquidity to people

seeking liquidity. However, some people might be surprised to learn that closed-end funds have historically required -- they have a 15 percent limit on illiquid investments unless all investors are accredited investors. This has been the approach of the SEC's Division of Investment Management. And recently staff have indicated that they are reexamining the staff position, which is something we definitely should encourage.

There is an additional requirement under the Investment Advisers Act which I don't plan to cover but where a fund is charging a performance fee, you also need to have a qualified client which has an additional financial requirement that falls somewhere between the accredited-investor financial requirement and the qualified-purchaser financial requirement.

Lastly, the 401(k) plan as an additional level of ERISA requirements need to be taken into account, including to prudently select and monitor any (break in audio) information letter setting out a framework and opening the door for target-date funds to have a portion of their investments in illiquid investments. That is a welcome improvement.

Just to give an idea of who qualifies an accredited investor on financial thresholds or a

qualified purchaser, it is estimated around 13 percent of households meet the accredited-investor definition and less than 2 percent meet the qualified-purchaser threshold. On 401(k) account balances, looking at the Fidelity data at the end of 2019, the average balance of a 401(k) account is $112,000. With about $233,000 out of 17.3 million accounts, around 1.35 percent having balances in excess of 1 million, let alone 5 million. As such, access to accredited-investor investments and qualified-purchaser investments is very restrictive.

Briefly, on design principles, as I said, we will be reaching out separately to get the feedback from AMAC members. We don't want to preempt the conclusion from the analysis of private investment returns, but we thought it would be good to get some guiding principles in place to help us come up with potential recommendations.

I won't cover all of these in the interest of time, but some of the design principles we have come up with include should access be only via a diversified pool. Here we mean a diversified pool of private investments, rather than a diverse-wide pool where there is some private investment. Should access be chaperoned by an intermediary? And should they act in a fiduciary capacity? Disclosure was a point that was earlier raised by Chairman Clayton. That is something else that we have picked up on. What kind of disclosure? Fee disclosure? What other disclosures? What restriction should there be on underlying investments? Should there be different shaded access, retail versus super retail? And should there be an incentive for funds that can show true market pricing in secondary trading? And, lastly, we talk about main street and retail investors, but who are we talking about exactly? Individual investors? We have seen the growth of IRA and 401(k)'s. It seems like they are a valid universe to also consider as many households' wealth are in the IRAs and 401(k) plans.

Lastly, I wanted to cover a couple of key terms that would be used in the panel: firstly, IRR. I wanted to cover this because IRR sometimes garners some controversy and some strong comments. Mathematically, IRR is relatively simple to explain. It is a discount rate that makes the net present value of cash flows equal to zero. It favors early cash flows. The example below of three investments with the same initial cash outlay but with different cash flows over time, they all have the same net present value and discount it at 8 percent and substantially similar multiples on investment capital between 2.25 and 2.8. The first

investment is equal cash flows over five years. The second investment back-ended cash flows in years four and five. And the first investment front-ended cash flows in years one and two. You can see a substantial difference in the IRR, ranging from 26 percent to 76 percent. So when using an IRR, one should always be conscious of its sensitivity to cash flow and its assumption of a reinvestment rate that might not be achievable.

Lastly, I want to touch on public market equivalent. You will hear the term "public market equivalent" being mentioned I am sure on the panel several times. At its core, public market equivalent is a relative simple concept of comparing returns for private investment to a public market benchmark. There are, however, several variants that are beyond the scope of today's discussion to fully cover.

I would quickly say, though, that the two types of public market equivalents you will hear is a ratio, such as the K-S PME ratio, where a ratio greater than one generally indicates a private investment that outperforms a public investment. The K-S PME ratio can be most easily described with a simple example of an investment with an initial capital call of 25, a year one cash flow of 15 and a year two net asset value of

20. In the meantime, the index has grown from 100 to 115 to 130.

Future value in those cash flows gives us the column marked in red. And the K-S PME is simply the future value of cash flows plus NAV. So the 20 and the 37 divided by 33, so 1.14.

The IRR we have discussed. The L-N PME effectively looks at the public market equivalent of that investment. So it says if you put 25 into the public market and then get 15 back at the end of year one, your NAV should be 16 in the public market at the end of year two and you do an IRR of that. And so your IRR from your private investment is 24 percent. Your IRR, effectively, from the L-N PME is 14 percent, indicating that the private market outperforms by 10 percent. A Direct Alpha is a similar approach but simply takes the IRR of the future value cash flows, so just the IRR of these red numbers.

I know that is a lot to take in, but I think the main message here is there might be a ratio or there might be a percentage number. When it is a percentage number, you have to decide whether you need to compare it to the private market to the public market, where there is a direct stand-alone number like Direct Alpha.

I have used up my 15 minutes. And, with that,

I want to spend the rest of the time on the panel. And so I will hand over to Erik Sirri and unshare my screen. Give me one sec to unshare. If a tech can help me unshare on their side? I have lost my WebEx screen. Thank you. Erik?

MR. SIRRI: Thank you, Rama.

And good morning. My name is Erik Sirri. I will be the moderator of the panel on private investment returns.

For investments in public securities like stocks, bonds, and mutual funds, returns are relatively straightforward to calculate. Methods for calculating these returns are sufficiently standard and customary that they can appear in mutual fund prospectuses, shareholder reports, and they can be used by investors for comparison purposes; for instance, either to other funds or to standardized benchmarks, like the S&P 500 or the Barclays Agg.

As Rama illustrated, returns to private investments can be difficult to calculate. And, unlike public returns, there is no universally accepted standard method for their calculation. Not only are accurate returns important for investors to judge relative fund performance, but reliable returns are required for investors to make portfolio risk and hedging decisions.

We are fortunate today to have with us four experts to help us on these issues. Two of our panelists are from the industry, where they specialize in private markets and the data that describe them. Our other two panelists are academic scholars whose research and expertise are in the private markets. We hope this panel will give you the audience a sense of both the complexity of the issues inherent in the private markets as well as a range of views held by sophisticated participants in these markets.

So let's jump right into the panel. I know I speak for Ed and the rest of the subcommittee when I say that we are very grateful for the time and energy these distinguished panelists have put into their presentations. Rather than give a full introduction to each of the panelists, let me refer you to their bios that appear on the SEC's AMAC website.

We have asked each of the panelists to speak for 7 to 10 minutes. We will then have some discussion among the panel members, after which we will open the floor up to discussions and questions from the entire AMAC.

With us today are Bryan Jenkins of Hamilton Lane, where he heads Private Market Analytics Group;

Noel O'Neil from Cambridge Associates, where he is the head of global investment research; Josh Lerner, the Jacob H. Schiff professor at Harvard Business School; and Ludovic Phalippou, professor of financial economics at the Said School of Oxford University.

With that, let me turn things over to our first panelist: Bryan Jenkins from Hamilton Lane. It is your floor, Bryan.

MR. JENKINS: Thank you, Erik. Just give me one second to share my screen here. Can everyone see my screen?

MR. SIRRI: Not yet. There it comes. Here we go. You are good.

MR. JENKINS: All right. So thank you, Erik. And I also want to thank the committee for inviting me here to speak on this panel today.

As Erik mentioned, my name is Bryan Jenkins. And I head up the research and analytics function at Hamilton Lane, where I specialize in the assessment of private markets data, portfolio strategy performance assessment, and the development of the firm's novel private markets industry dataset.

So I do want to spend just a quick minute on Hamilton Lane for any of the committee members who are not familiar with our firm. We are a private markets

investment firm. We have been investing in private markets for over 30 years. Private markets is all we do. Now, private markets is more than just private equity. It also encompasses private credit as well as private real estate and private real assets, so infrastructure and natural resources.

Across those strategies, we manage or advise on over half a trillion dollars worth of assets as of June 30th, 2020. And those assets are across primary fund commitments to new private equity funds; secondary transactions, so purchases of seasoned or mature interests in private equity funds; as well as direct investments into public companies.

Last year, we deployed over $33 billion worth of capital into private investments on behalf of our clients, which we think makes us one of the largest allocators of private capital in the world. So we serve over 600 clients, mostly sophisticated, thoughtful institutional investors. And it is really a broad cross-section of investor types. So we serve pension plans, both private and public, large and small; Taft-Hartley plans; financial institution; sovereign wealth funds; endowments and charitable foundations; family offices of high-net-worth individuals. And those clients have varying degrees of familiarity with private

assets when they first engage Hamilton Lane. Some have been investing in private markets for decades and have an experienced staff. Others may have dabbled in venture capital during the rebellious stage in their early aughts and have leading familiarity with private assets. And others are de novo investors in private markets and really seeking answers to some of the same questions that this committee is looking to get answered here today. So we think we are in a unique position to assist those investors by providing data and analysis to support their decisions to invest in private markets. So because of our platform, because of our position in the industry, we have one of the most unique and comprehensive and, most importantly, one of the highest-quality datasets in the industry. And this is in an asset class where quality data has historically been very difficult to come by. Actually, between the Hamilton Lane dataset and the Cambridge Associates dataset, which will be represented by one of my co-panelists, you have two of the finest highest-quality datasets in the industry in front of you on the panel today. We are tracking trillions of assets, thousands of funds, tens of thousands of companies. I think, importantly, all of this information comes from financial statements that LPs are receiving, so from the valuation statements, audited reports, cash flow notices. That information is checked. It is audited. It is rigorously QCed. And, most importantly, it is representative of what institutional LPs have been investing in.

So I included page 5 here for reference for the committee. Rama touched on some of this in his introduction. We will probably come back to some of this during the open discussion. So I don't want to spend too much time here but a couple of quick points. First, as Rama and Erik alluded to in their introduction, comparisons between private market returns and public market returns can be challenging because the way returns are measured is different in each of those asset classes, IRR for private markets, usually a time-weighted return for public markets.

Number two, the way that we get around some of those challenges is by using a public market equivalent. So Rama went over some of the different flavors of public market equivalent in his introduction. That is generally the method that we prefer to make comparisons between private asset performance and public markets.

And, third, while PME, public market equivalents, are our preferred comparison methodology, there are other metrics that investors are using to

assess performance in private markets. So I wanted to make the committee aware that there are other techniques besides public market equivalents that some investors use.

On page 6, I am showing one of the most standard ways to look at performance data in private markets. So what we are looking at are the vintage year returns of private equity. So private equity here is buyout funds, venture capital funds, and growth equity funds. And so private equity funds are typically grouped by vintage year or the year that they began investing. So each of those blue bars is representative of the performance of funds that began investing in that year through Q4 2019, which is the as-of date of this performance. So these are not calendar-year returns. And also, for avoidance of doubt, all of the private equity performance shown on this slide as well as subsequent slides are net of fees charged by general partners, so management fees as well as performance fees.

So each of the dots on this page represents a public market equivalent, PME. And we have selected three indices here for comparison. The first is the MSCI World Global Equity Index. A lot of institutional investors look at this as an opportunity cost benchmark.

If they were not deploying capital in the private equity, they would likely otherwise be deploying it into traded assets, likely their traded equity book, which nowadays tends to be very global and often mirrors the geographic allocation of the MSCI world.

Second, we have the S&P 500 historically used for comparisons, still favored by some North America focused investors who are primarily investing in U.S.-focused funds.

And, then, third, we have a Small Cap Value Index here. So there have been some arguments that small cap value stocks are closer to the types of companies that are targeted by private investment funds in terms of enterprise value as well as having the value tilt.

We have those three indices here for performance comparisons. The general themes are consistent, regardless of the index you look at. In the 19 vintage years that we are seeing here, performance of private equity has been pretty good relative to public markets, so outperforming the global equity benchmark by about 500 basis points on average across these vintage years.

The S&P 500 Small Cap Value Index, there are some vintages where performance has been about the same

as those two indices, mostly concentrated around the global financial crisis, but in most of the vintage years through this time period, including more recent vintage years, private equity is posted attracted performance. If you had begun investing in private equity in 2011, you would have achieved a 300 basis point premium to the S&P 500.

And, then, last, I would point out the comparison to value, small cap value, stocks. This is something that in the '90s and early 2000s, small cap value performance looked pretty favorable against private equity, but in more recent years, the performance gap between private equity and the small cap value stocks has widened, so potentially some additional factors to explain private equity performance.

Page 7 here, a slightly different view of performance. Some investors like to look at performance over various time horizons, grouping all vintage years together, looking at performance over one, three, five, 10, sometimes 20 or 25 years.

So what we are showing here is performance on a rolling 10-year basis, 15 years shown on the chart, really 25 years worth of data. And I think some of the themes are similar to what you see on the previous page. Consistent outperformance of global equities, the performance gap against U.S. equities, as well as small cap equities is narrower. And I think, different from the previous page, there is a period more recently where some traded equity performance has approached private equity performance and even briefly eclipsed it. I think it is interesting to reflect on the conditions under which that occurred. So if you think about the time period, it is a 10-year period starting at the trough of the financial crisis and culminating at the peak of a 10-year bull market that has been really booming by loose monetary policy that it has pushed up valuations in both traded assets as well as private assets.

And then also consider that for the 10-year returns in 2018 and 2019, for private equity, that is right about average, around 13 percent. Those returns for traded assets would be towards the higher end of their distributions. Certainly a 15 percent return for U.S. equities would be at the higher end of the distribution for 10-year returns.

So I am coming up close to my time. So I will just flip quickly through these last few slides, and we can come back to these if people have questions in the Q&A session.

Page 8, I just wanted to quickly highlight

that private markets is more than just private equity. About 60 to 70 percent of the market is venture capital and buyout funds. The other 30 to 40 percent are things like private credit. Some of these funds have stepped in to lend to middle market companies, where banks have been treated, as well as private real estate and infrastructure and natural resources. And they are a significant portion of the nearly $6 trillion of AUM in this asset class.

And then I will just skip to the last slide here. What are showing on page 10, we looked at 5-year returns over the last 25 years and picked the lowest 5 year return for each of these assets, so both private assets as well as traded assets. So it gives you a sense of some of the potential downside in a worst-case scenario over a five-year hold period.

So for developed market buyouts, that worst-case scenario, is about 2.4 percent, so nothing to write home about, certainly well below what we would generally target for buyout returns but on a leg-for-leg comparison basis to the MSCI world, a bit out of that.

Now, venture capital, the downside there is certainly a lot higher. I think most would expect that given the risk profile of that asset class. And that downside return was around the dot-com bubble.

And, last before I cede my time to the next panelist on private credit, that asset class is the private equity strategy that has the smallest difference and the worst-case return from its long-term average return. So the difference in average return to worst case is narrowest there. And so I think that says something about the consistency of the return in private credit, even though that is a relatively younger asset class.

So I think I am pushing up against my 10 minutes. So I will cede the virtual podium to the next presenter.

MR. SIRRI: Bryan, thank you very much. So if you will unshare your screen? And Noel, our next speaker is Noel O'Neil from Cambridge Associates.

MS. O'NEIL: All right. I needed to unmute myself there. Let me share so can you all see my sorry about that little technical challenge there.

Thank you for the time to speak with you today, very much appreciate the opportunity. I am Noel O'Neil. I am president of the Cambridge Associates. I lead all of our global investment activity, both private equity and non-private equity.

Cambridge Associates, just a brief background. We have been in existence since the mid 1970s. We

manage or advise on our $400 billion of investment portfolios for about 900 institutional clients across endowments and foundations, pension funds, and large family offices.

We have been involved in on behalf of our clients investing in private equity, venture capital, and other private investment areas, as Bryan described, since roughly 1980, starting in venture capital first in U.S., then in private equity or the buyout area in the mid 1980s, and subsequently outside of the U.S. in Europe, Asia, et cetera.

In other to be more effective investors, we started a process early on of collecting the data from venture capital and private equity funds. That is the dataset that I am going to use today to share some of the insights we have on the questions of both investment return from private investments as well as risk indicators.

Similar to Bryan, though, the dataset that we have is actually very, very similar to the dataset that Hamilton Lane has, goes back to, as I said, early 1980s, covers about 8,000 separate funds, a little over 8,000 funds that we have collected data on, many of which have completed their lifecycle. So the full investment period of money going in, money coming out is long, long finished. And, then, aggregate, the aggregate commitments in those funds was close to $6 trillion. So it is a fairly substantial history of viewing private investments across a variety of asset classes, both venture capital and leveraged buyouts, as well as private credit, et cetera.

I wanted to with these first couple of exhibits address something similar to what Bryan addressed, which is the return from private investments relative to public equity markets. This first chart has what we call private equity, which is primarily leveraged buyouts, does not include venture capital, for example; does not include private credit; et cetera.

And this just shows the annualized returns over long periods of time. So the private equity is in the blue. This goes back 30 years. And we have two public equity market reference points in here: the S&P 500 and the Russell 3000. And the cap as here is using MPME, as Rama described earlier, essentially a methodology to take the same cash flows that were invested in private equity and put them into the public equity markets.

As you will see, the longer-term returns premium from investing in private equity is quite significant over the public equity markets, but this

also shows them you know, one of Bryan's chart shows that premium spread versus public equity markets has been much less in recent periods, in part, because, as Bryan mentioned, the public equity market returns have been very strong post-financial crisis. But I would say also because the amount of capital being invested in private markets has grown steadily over these periods. And the industry has become more competitive.

The next chart basically highlights the same information for venture capital. In this case, we are comparing the venture capital returns against both the S&P 500 as well as NASDAQ. It is very debatable what is an appropriate public equity benchmark for venture capital. And we have often looked at much smaller cap benchmarks, like Russell 2000 growth, for example, or even sector benchmarks that are more focused on technology. But, anyway, a key observation from this data is that long-term venture capital returns were very, very strong events, public equity markets, particularly in the late '90s. In the recent decades, while they have been very strong compared, for example, to the NASDAQ Index, which is, you know, heavily influenced by some big tech companies, as you know, the private venture capital investments have actually lagged over shorter periods.

The next point I wanted to address is a way of thinking about risk. In public equities and in public investments that are listed and priced every day, investors, we included, use standard deviation return, for example, as an indication of risk. In private equity and private investments broadly, standard deviation isn't that useful a tool because of the lack of real mark-to-market. So one of the ways we look at risk is dispersion of returns. So this chart shows in this case, I am just using private equity as an example that the dispersion is similar in venture actually wider in venture capital, and dispersion is much less, as Bryan mentioned, in areas like private credit. But what this data illustrates is that the difference between the top-performing funds in any given size range so the bars here go from small, less than $200 million, sized private equity funds to on the right the very largest and most commonly known mega private equity funds that are over $10 billion in size. Two key points on this. One is that there is a wide level of dispersion between the top-performing funds and the bottom. Second is the bottom you actually can lose in the smaller bond sizes. And to one of the points Robyn made earlier, I think it does emphasize the need for diversification in making private equity investments,

particularly if that is going to be available to smaller investors.

A related point on this next chart, but I wanted to contrast what that dispersion looks like for private equity areas, which is the right three columns here. So the first to the right in green is "Global Venture Capital." The next one from the right is "Global Private Equity," and we included private real estate as a reference point in here as well. A key point on this chart is dispersion, meaning the difference between return earned by the median or average fund versus the return earned by the top quartile or 50 percentile in this case, is much, much wider than it is for the asset classes on the left. So the asset classes on the left, you know, there are various types of public equities and fixed income.

And this dispersion is for active manager strategies in those areas. For example, in U.S. large cap core, you know, the dispersion between a top quartile or 50th percentile fund versus the median is quite narrow.

The other very significant difference between the left and the right side of this chart is that the left-side investors and this is a very important point for retail investors is you have a passive investment option. You can elect to invest in the market and not pay active fees. In the private investment markets, there is no passive option. You have to invest actively. You have to pick someone to make the investments for you. And so our point is the dispersion on how well people do is a very important thing, which means selecting who it is you are private equity investing on your behalf is very important.

I also wanted to briefly address one of the questions Rama raised, which is around the degree to which private investments provide diversification value. This chart gives a summary of some statistical correlation data between various categories of private equity funds so that Mega Cap those are the really big funds, all the way down to sort of small, or PE, funds, which can be as small as $200 million in fund size and compares that to some public equity indices, the S&P, Russell 2000, ACWI, et cetera.

Now, I would be the first to say that using correlation data with private equity is limited, at best, in that private equity valuations are not done anything like sort of the frequency or effectiveness of the public equity markets. So any look at correlation data necessarily needs a caveat. The broad point that this makes is that there is more diversification value

as you get away from the largest types of (audio distorted) funds and get to smaller, more focused funds and particularly I don't have the data here, but I will address it separately as well later that in subsets of private investments, like, for example, let's say, particularly venture capital, where the cycle of investments and the (audio distorted) those investments are very different from the broad economy, but those areas of private investing can provide meaningful diversification to a typical public equity portfolio.

And, just to expand on that point a little bit I think Bryan had a somewhat similar chart that when people know about private investments or even loosely the term "private equity," sometimes we get that there is a very broad swath of different types of private investments out there.

We use this chart just to sort of illustrate that what we think is a lengthy (audio distorted) between the types of private investments and the sort of overall performance of the economy. So in the center of this chart and by far the biggest category of private investment, which is leveraged buyouts for private equity that are we would say largely (audio distorted) linked to GDP in broader economic cycles; whereas, the further you can get away from that, particularly, for

example, on the right side of this chart, where we talk about venture capital, early-stage venture investments in, for example, technology and biotechnology, information technology, biotechnology, you know, are subject to sort of economic influences that make their performance quite different from the broader economy and, therefore, different to some significant extent from global public equity markets.

So from a diversification point of view, think those areas have more diversification value. I would say I think mainstream buyouts provides very limited diversification value to a typical public equity portfolio.

Those were the main points I wanted to raise. You know, I would just say, in summary, we think private equity has provided extra return over public equities and public equity markets in the past. That spread or benefit clearly is getting eroded to some degree as private equity has become a larger and larger area, more competition. You know, we still think for investors who have the capacity to invest with the best private equity firms and know how to find those, it is still an attractive area but not something to get involved in unless you feel like you have the capability to do the appropriate due diligence, et cetera.

Let me stop there and hand it back to you, Erik, and the next speaker.

MR. SIRRI: Noel, thank you very much. This is very helpful. So if you will unshare? Great.

Our next speaker is Josh Lerner from Harvard Business School.

MR. LERNER: Thank you, Erik. And thank you to the committee for the chance to talk here.

I was looking over my slides last night, and I must admit I felt a little bit resonance with the old story of Harry Truman and his search for a one-armed member of a Council of Economic Advisers because he never wanted to hear economists saying, "On the one hand," "On the other hand." I am afraid I am somewhat guilty of that in this talk. But, hopefully, at least some of the considerations I raise here will be helpful for the committee in their thoughts around these issues.

So, anyway, I have been doing this for a long time and certainly written a lot of cases on a lot of private equity groups, worked with limited partners, general partners, as well as government bodies around this. I don't consider myself to have a dog in this fight but just for full disclosure.

And, as I mentioned, these are some big questions, but I thought that sort of taking some fact-based approach here and highlighting a few key things that might be germane for the subcommittee in terms of weighing these issues might be helpful.

The first is that I do think that, as was sort of alluded to before, there are some you know, you can certainly make a case that there are some potential diversification benefits from private equity and that certainly to the extent that it made sense in a portfolio of a pension plan, defined-benefit pension plan, it might make sense for an individual investor as well.

Perhaps the most powerful case, at least in my view, for this is a paper that my fellow panelist Ludo wrote in our top journal, Journal of Finance, 18 months ago or so with Andrew Ang and Will Geotzmann, where they basically argued that private equity did have a set of characteristics, a set of factors, to use the finance lingo, that was different from that seen in the public market in that one could get substantial diversification from it, not just simply private equity versus the other stuff but also even within the different classes of private equity.

So that is really the one hand, but, on the other hand, there is a set of things that have already been hinted at. You know, certainly one of them is the

relatively little outperformance that private equity has generated. As you look at recent vintage years relative to the public markets, essentially this is Preqin's data, but I think it looks very similar to the data we saw from my prior panelists, that, essentially, there has not been much. There are some PMEs. They have been above one in general but not by much and that, certainly, it doesn't seem like that there is a huge amount of juice in the lemon in terms of outperformance that is there.

Another fairly stark way to look at it is to look at just the absolute performance. So this essentially is TVPI by vintage year. And we could take this back a couple of more decades and make the point even more dramatically that while there have been ups and downs, the general trend has been downward, which presumably reflects to a certain extent, as Noel alluded to, the increased intensification of competition in this sector. So this is concerning enough, but there is a sort of added issue out there which has to do with fees, particularly fees in the context of retail products.

The kind of analyses we saw over here from Preqin or in this case from Cambridge are essentially looking at the returns garnered by an institutional investor, who is presumably paying the sort of standard

2-and-20-type arrangement. But we know that, at least historically, the retail products that have been offered have had another layer of fee on top of that, which in some cases has been sales loads or management fees, backend charges, and so forth. I just threw a few examples up here garnered from media accounts, but, in general, I do think that that I mean, we might plausibly worry that in these cases, adding another layer of fees on top of it for retail investors would take whatever limited juice was there and basically take away all of the alpha.

Another consideration which has been raised, at least that I have heard raised, in some of these discussions has been about the fact that, you know, not all investments are done through funds. And, in particular, we know that there has been a lot of interest in doing co-investments. Co-investments are reasonably attractive at many levels, not the least of which is that in many cases, they are being done on a no-fee/no-carry, or low-fee/low-carry basis. And, as a result, they avoid some of the fee drag, which occurs otherwise, because I think that, certainly, we would all agree that private equity on a gross basis looks very attractive. It is just that simply the overlay of the 2 and 20, which sort of brought those numbers back down to

Earth.

So, essentially, here in this chart on the right, we illustrate our working with another data source, that of State Street, which in their custodial role would essentially see all of the cash flows that they institutions, the limited partners they have relationships with make. And, as a result, it sort of illustrates that for State Street's institutions, their private equity commitments have gone from the share that is in the form of co-investments or other non-fund-type investments has gone from on the order of 2 or 3 percent that characterized it during the 1980s or the first half of the '90s to a much more dramatic level. And, in fact, in the last year of our analysis, 2017, it represented almost 40 percent of the money going on, not in the form of funds but through these alternative vehicles.

You might say this really helps address some of these concerns. The challenge is that when you look in the long term, what one sees is that the co investments in other kinds of alternative vehicles haven't really done that well. And here we are essentially comparing apples to apples. So we are saying, if you invested in a deal, what would have been the returns you have gotten from that co-investment, again, any kind of modest fees that might be charged relative to the net returns you have gotten from investing in the corresponding fund?

And you might think that it is a no-brainer that you are going to outperform from the co-investment simply because you are not paying fees, but, as one sees in the top line at least, over the long haul, in actuality, people have underperformed in those investment. And you might say, "How can this be?" Well, a lot of it seems to really stem from what one might term "adverse selection issues," that many of the co-investments get concentrated around market peaks in many of the biggest deals. There are any number of logical reasons why that might be, but the end game is that it doesn't seem that one has that this seems to be a very clear route for outperformance.

Now, again, on the other hand, when you look at the most recent period, particularly the years after the global financial crisis, one does have a significantly better performance here. But, in general, the co-investments have been tough and challenging, a challenging area.

So I guess in some sense, I feel taking stock of research and trying to assess it, it is a little bit like some of the research that we talked about last year

on the employment and economic impact of private equity. It really seemed to satisfy no one in the sense that I think there are some considerations, on the one hand, that perhaps make a logical case for why this may make sense, but there also a number of important considerations here.

So, in any case, hopefully laying out some of this data will be helpful to the subcommittee as it undergoes its deliberations around this process. And, with that, I will unshare myself and turn it over to Erik.

MR. SIRRI: Perfect, Josh. Thank you so much.

Our final panelist will be Ludovic Phalippou from Oxford University.

MR. PHALIPPOU: Thank you for having me. I am going to share my presentation.

Do you see it? I think you are all right?

MR. BERNARD: Yeah, we got it.

MR. SIRRI: Yes, we see it.

MR. PHALIPPOU: All right. I am not going to talk about performance, per se, performance evidence. I've written about it in a book, in a paper recently. And wouldn't want to repeat largely what Josh just said. And for me to explain why, what you hear from petitioner presentations -- so the one of Hamilton Lane,

of Cambridge Associates, and the conclusions that I reach using the same data, it would take me quite a while. So we could do such an exercise, but separately. Here in my seven minutes, instead, I wanted to focus on how private equity firms present their track records. In this presentation, I'm not going to make any assumptions, no calculations. I'm just going to show you things that we see in practice and I'm going to comment on them.

In fact, my career in private equity started 20 years ago when I was a PhD student and I knew nothing. And somebody, well a fellow PhD student called Oliver Gottschalg, showed me what he thought was a bit of trickery. He said look, I have here a bunch of fundraising prospectuses from private equity firms. It's a track record about -- of -- abut any private equity firm in the world.

And you can see here all that data about their past returns, et cetera. And he was basically the only one to have collected such data there in the early 2000s. And when I started reading these documents, I was in a state of shock. The documents said it was confidential everywhere. And I couldn't take my eyes off the footnotes that were basically saying that the track records were selected, for example, over there

were some gross of fees, over there were some weird performance measures, like Time Zero IRR. And there were some Since Inception IRRs that were not making any sense. It was just shocking.

And I tried to describe a bit what I was seeing in some early papers. But my colleagues didn't really know this data. They hadn't seen them, except probably for Josh. It was hard to get traction and nobody basically believed me. People said, "Look, it's all sophisticated investors. They can get all the data they want. We do all the calculations. So there's no point in you whining that like fundraising prospectuses are misleading or things like that. This is -- you're just impossible." Okay?

And it just turns out that a few weeks ago, and I think for the first time, one such presentation of private equity fund track records, ended up -- a fundraising presentation ended up in the public domain. And so I thought, you know, I'm going to share that with you, because it looks very much like the ones I've been seeing for 20 years. And it is one of these presentations that does shock me.

And so I'm going to show you a bit the sort of information that people investing in private equity are presented with. And I think this is very relevant for the SEC, and that's why I'm doing it. Because the SEC, I think, has always been very interested in understanding how track records were presented to the public. And the SEC has a long history of trying to make track records presentable in a way that was fair and meaningful in all the fields.

So I was asked to anonymize this company, so they are called "TBN", okay? And this is their first slide, okay? They say, look, "This is us at a glance. Strong performance. Experienced Organization. An expanding market in which we invest. A different strategy and a reputable process. We have invested zillions under management" and blah, blah, blah. Okay? That's their first slide.

Here are a few remarks about this first slide, about this firm at a glance. So it's a presentation that's publicly available. It was made to public pension funds. The one of Rhode Island here, just in June this year.

First remark is that the returns are presented gross of fees, which can be a bit surprising. I think it's important for people to have orders of magnitudes of what fees are in private equity, because 220 sounds a bit abstract; it doesn't sound that much. But what it means when you convert into an annual rate, that would

be similar to an expense ratio that you would see in the mutual fund space, the average private equity fund charges six to seven percent a year, okay? So we are talking about fees that are three to four times the magnitude of mutual fund fees. I think that's very important to have these numbers well in mind. Okay?

At first here -- a 50 percent gross IRR net would probably be at 25 or 30, but an IRR is not a rate of return, so that's not useful. But anyway, but the first thing is to note is that we are presented numbers as gross of fees in a very high fee asset class, so to me it's surprising.

The second thing is this IRR. We heard earlier that you need to be careful with IRR and so on. It's not that you need to be careful, it's that this number makes absolutely no sense. It's not about being careful, it's about banning it. When a firm like this tells you, I have 50 percent return, most people think like oh, wow, it's like 50 percent like rate of return on money. Like, this is just amazing. Yeah, it would be amazing.

Because somebody -- this track record is 20 years long. If somebody had earned 20 years 50 percent a year, they would have multiplied money by 3,300. And they have "zillions", which is about 7 billion, would

have become 24 trillion, okay? So if a private equity firm like this one would have transformed 7 billion into 24 trillion, I think you would have noticed. If people don't know what 24 trillion means, it's basically like the GDP of the U.S., and you would need to add Japan to it, because you wouldn't get quite there yet, okay?

So the multiple of money is quite high. So a bit of a better measure -- but we, knowing the effective duration of cash flow is pretty empty as well. But what's most amazing to me is that the track record is selective, you know. Like if you have a mutual fund, or like any investment manager, you're not allowed to show a selected track record. We completely know that it's too easy to just select your investments and just like present this as your track record.

And the way it's done in private equity is as follows: the first thing is to say -- written here is a footnote, number one, of the realized returns. You say, oh, that's, you know, sense enough. But except, if you can realize your winner, and you hold onto your losers, then your realized returns will always look amazing. So that's very, very selective. That's very, very biased.

Then you say in software -- so then, you know, imagine you invested in different industries. You picked the industry that looked the best, and you say

that's what you recall in that industry on mine. Imagine a mutual fund manager allowed to do the same thing. A mutual fund manager having losing positions. Hold on to these positions. Winning positions they sell. They just show you their realized investments. And they show you only the ones in the industry of your choice.

On top of that, there is this other thing that is there in many, many track records. This is the track record of people that are still in our staff. So imagine that Josh and I are working for TBN. Josh does only amazing investments. I do only bad investments. They fire me. They keep Josh. The track record looks amazing. And again, it sounds pretty innocent. It's like, you know, if Josh was better, so they kept him, because his track record looked so good. Except, if exposed, you can say, well this investment didn't do quite well. We're going to put this one on Ludo. And this one did pretty well. We're going to put that one on Josh. And we are firing Ludo and oh, all the bad investments are gone. All right?

This is pretty extraordinary. It's also pretty extraordinary that you are allowed very often -- and you see that in many track records -- to take investments that you've done in your previous job and say, well, actually I was responsible for that great investment in my previous job, but this one that didn't go well I wasn't really responsible, so that's not going to count on my track record. So you just cherry pick.

I mean, if these are the rules of the game, you can just like, manufacture the most amazing track records out of thin air, okay? To have a bad track record, you should really like work very hard, okay. And again, it's like, if you would tell mutual funds you can play with these rules, they -- you know, it would be jaw-dropping for them, okay? Like, they would think like it's Christmas, okay.

So this -- this is a presentation shown to so-called sophisticated investors. But people have been saying, look, they know what they are doing, people are smart, blah, blah, blah. You're just, you know, talking nonsense. My question is, if people are that smart and that sophisticated, why are they treated like idiots? Because if such a presentation would be shown in my college endowment, the person would pretty quickly be put on the spot and feel ashamed show something like this. If they are not feeling ashamed, they are feeling free to show that to public pension funds, it means that some people are influenced by these kind of misleading numbers.

Now, this one very quickly, that's like slide number two or three. If I show you this, I bet you that what you thought is that what this means is that what this TBN form does is they take money with EBITDA margins of minus three percent, and they grow it, hence the rising arrow, to 38 percent average margin in their portfolio. You would think that. You would think they have companies that have zero to 10 percent margin and bring them to 38.

You read the footnotes. It just happens that the minus three and 10 percent is the margin of some public firms in the software industry. And 38 percent is the margin in their portfolio. These numbers have nothing to do with one another. They're just put there on the graph, a rising arrow, and bingo. That's our value creation advantage.

Again, go back to the sophistication argument. If you are talking to somebody sophisticated, why do you show things like this, that makes absolutely zero sense?

That's where a correct track record -- I probably don't have much time to go over this -- would just highlight that basically, depending on their holding period, we could think that their actual true return is probably something like 23 percent net of

fees. And that happens to be what publicly traded software have done in the U.S. I could only go back 10 years, because there was no indices before in software. But again, to show you that benchmark is not trivial. And if you do it properly, very often you find that, you know, reality is very different from what is shown in these fundraising prospectuses.

And so that's a bit tricky, because as the SEC has been concerned for nearly a hundred years now, you want to be sure that when people are presented any investment opportunity, they are presented things that are kind of adding up and making sense.

Now, I'm going to continue with showing you an example that is in SEC filings, by the way these firms present themselves. In fact, a firm here that I call B4-A is one of the big four firms, okay, and it's going to be A. So A says this in their SEC filings. They say, they were founded in the 1990s, early 1990s -- they say, "We generated 39 percent gross IRR and 25 percent net as of end of 2019." So basically over 30 years' period, that's our return. In fact there was a board member of this company that came to our academy conference once, and very, you know, proudly, announced that, "You know, we just raised the largest fund ever in private equity. But no wonder we did. We generated 39

percent return over 30 years' period." I mean, who would believe that, right?

So this guy was saying we raised so much money because we generated 39 percent return over 30 years. Who would believe this? And of course, you know, my grandma hearing something like this would be very excited. The problem is that my grandma doesn't know that IRR is a completely fictious number. She doesn't know that, okay?

So same thing for another one that I called Big4-B. These guys, they started even earlier. They're actually exactly my age. So I know that they are exactly 44. And they have a 26 percent return over 44 years. Which, they don't mind comparing to a geometric average of a public market return. These two things have nothing to do with one another, an IRR and geometric average of the public index. But they don't mind. And they show these numbers.

So just to note for one's selves, if these guys, Big4-A, okay, had earned 39 percent -- which on just one billion dollars -- they have much more under management, okay. But just one billion dollars, 39 percent over 30 years, they would have returned 20 trillion. Remember, that's the GDP of the U.S. So my grandmother would get very excited with 39 percent return. No wonder she's excited. Somebody's basically telling her that they transformed 1 billion into the GPD of the U.S. over 30 years' period.

The problem is that it's obviously not true. This firm actually, for every one dollar invested, they revert -- they report only gross returns -- they revert 1.8 times gross. So net is like 1.5, which happens to be like public market returns, okay?

For the other one, same thing. 26 percent over 45 years, actually there it's even more than the GDP of the U.S. Actually half of the planet Earth's GDP. So somebody is writing on SEC forms, "Look, I've been, over the last 45 years, I've returned 26 percent gross." And that person is basically telling you that the one billion would have been converted into half of the Earth's GDP. And you know, that's cool. You know, it just -- put these numbers like that, people get very impressed, and that's all allowed.

MR. SIRRI: Ludovic, I cut you off. But I wanted -- can you wrap up? I want to be sure we have time for discussion.

MR. PHALIPPOU: Yeah. It's my -- it's kind of my last slide. And this number really is like super high and super meaningless. Not only that, but on top of that, never changes. So I put together this thing.

The one on the left hand side is every form filed with the SEC by my Big4-B. And you can see that there are 76 to 96 funds that had a 26 percent net IR. And this number, number never changes, ever since 1996. So every year they tell you they have the return. Okay? That would make some people very, very jealous, okay? And a number of people would question how on Earth is this allowed, okay?

And the second one is my Big4-A firm. Same thing, number never changes. And there is year end amount; also the number never changes. I pointed this out in a paper in 2014. Since then they changed their format. But they still report same IR, but that's very misleading to people. So again, if the sophisticated investor argument held true, I don't quite understand why people would be presented with these sorts of information. This information is always kept confidential. Nobody's allowed to look at it, not even for research, and so on. And you really wonder whether it's confidential because it contains a Coca Cola recipe, or whether it's just very embarrassing when put in daylight.

Again, remember that these fees are very high, and many people make a very good living out of these very, very, very high fees, and have all the reasons in

the world not to present to you fair and balanced evidence.

So my focus would be the most relevant for the SEC to know, especially given the track record of the SEC of tracing, particularly in the mutual fund space, all the deceiving way that people have found to present track records to their investors. Thank you very much.

MR. SIRRI: Ludo, thank you very much. That was very insightful. So maybe to start things off, let me loop back to Josh. Josh, you used a PME measure in your work; other reports have presented rates using IRR. Josh, in your view, how should the SEC approach the question of what information private investment managers should give to retail investors, when it comes to performance and risk?

MR. LERNER: Well, first of all I want to say that I do share Ludo's unhappiness with the IRR as a measure. And we can, you know, sort of talk about any number of examples. But you know, just one of a number of odious aspects of the IRR he didn't mention is that you can actually end up with multiple routes. I remember an instance a few years ago where there was a venture fund that he had the LP started, he had an IRR measure of 10 percent. The GPs had it, thought it was 30 percent. And the answer was that they were both

right. Because basically when you get inflows and outflows you can actually get multiple IRRs for the same, same funds. So this is a very tricky kind of measure which, while it's widely used, is not without its problematic aspects.

That being said, you know, I tend to be a fan of the Big 10's approach, which is to say, you know, what you'd really like to do is to say let's convey, look at as many different metrics as one can, including PMEs, including, you know, mutiples and so forth to try to get a sense of, you know, grounding in reality. That any one measure may be problematic for a variety of reasons, but taken together one should get a -- or potentially a clearer view of what it looks like.

MR. SIRRI: Noel or Bryan, do you want to jump in on this?

MR. JENKINS: Yeah, sure. I'm happy to jump in. I think we're in agreement with Josh's, I think he called it the Big 10 approach, of looking at a number of different metrics. And I -- you know, I think I agree with Ludo in that the transparency in this industry could be much improved, yeah, for when we are evaluating funds. In addition to, you know, the marketing documents, we're also getting full attribution on the deals or on the full cash flows, cash flows for each deal. And so we're able to do a type of analysis that is difficult to do off of just what's provided in a marketing document.

So I think having some of that information available will make some of the performance comparisons a little more transparent.

MR. O'NEIL: I'd agree with Josh as well, on that you have to look at more than just one measure. And two quick comments on Ludo's points. One is I totally agree with him that marketing of track records by private equity GPs can be incredibly misleading and misrepresentative, and very commonly, for the reasons he cited, by using both gross numbers and selectively including or excluding. And so you know, that's something we always look very carefully at. And the second point he made, which is one I meant to make at the end of my presentation -- I have a chart in my deck that you could refer to later. And that, just reinforcing his observation that fees in private equity are very high. We would measure that over time, and it's very supportive of the 600 to 700 basis points that Ludo referred to. And it's you know, private equity returns at a gross level would have to be very high to support that level of fees and still be attractive to investors.

And you know, one of the things that we've been waiting to see over time, which we haven't seen enough of yet, is pressure on GPs to reduce fees. And we certainly try very hard to apply that pressure ourselves, but it's -- you know, we're limited by the sort of supply and demand of the industry.

MR. SIRRI: Okay, thank you. Let me turn to something we -- I don't think anyone mentioned, and that's liquidity. You know, the comparisons were made to these public benchmarks like the S&P 500 or Wilshire or something like that. But those are fairly liquid securities that underlie those benchmarks. Not so for private investments. Are investors going to be fairly compensated for bearing this liquidity risk in your view? I'll throw that open to the group.

MR. JENKINS: Sure. I'm happy to kick off with this one. They were thinking on the liquidity premium that investors should demand, and they should demand a liquidity premium for holding these assets that, you know, on average are held for six years. And the life of the fund often expands, 10, 12, 15 years. Sometimes beyond that. The liquidity premium that investors should demand should partially depend on the duration of their liabilities. And so there's certainly some institutional LPs that take the approach that they

don't necessarily have short-term liabilities. They're a -- we're taking a longer-term view. And they tend to think about their liquidity premium as being smaller than say a retail investor. You know, 55 years old and a few years away from retirement, you might want to demand a higher liquidity premium for your time in assets that they may need to access in the short term.

MR. SIRRI: Does anyone else want to comment on liquidity?

MR. LERNER: Ludo -- I mean, I don't.

MR. SIRRI: Go ahead, Josh.

MR. LERNER: No, I was just saying Ludo wrote an article on this exact subject, so he should say something.

MR. SIRRI: All right, Ludo. You're on.

MR. PHALIPPOU: Yeah. I think when it's a small part are above 40, it shouldn't command that big of a premium. But we need to be careful with the withdrawals that retail investors may need. But when we look at the retails like I did in my paper, they look pretty close to many public market indices. Of course you can choose indices where it looks better. So we've seen that in some presentations. If you choose MSCI World indices, or it is particularly is mainly U.S. and the U.S. Dollar also appreciated, you would get a

different picture than if you choose like small cap, mid cap U.S. stocks as benchmarks, et cetera. So when you look at indices that are closer to what private equity does that doesn't look like there is much out-performance to begin with. Going forward as well, given that the expected returns are generally lower, the fee structure in private equity is such that it's pretty hard to see how there could be any premium anyway.

MR. SIRRI: All right. Josh mentioned the term Adverse Selection. And you know, one of the things that it seems to me is true about these kinds of assets is that a small fraction of investments could provide a lion's share of returns in a pool. That's not true of something like the S&P 500. Do you think that poses a challenge in any way for the Commission as they value how to structure or regulate these investments? The effective cross-sectional skew in where their returns are?

MR. NEIL: Maybe a brief comment, Erik. That skew, as you described, is particular noticeable in venture capital, in technology, where the -- you know, I'm unsure -- average venture capital returns, but the skew is very extreme, and a small percent of the venture capital deals and venture capital funds generate a very large amount of aggregate profit. I think that is particularly relevant in that it makes it very difficult to be able to broadly invest in that asset class if you don't think you can access that subset of investments that would generate those returns. The skew in our experience is much less so in mainstream private equity or buyouts, and not that different from public equity markets.

MR. JENKINS: Yeah, I would agree with Noel's comments. I think someone else's that we've done have supported that. And it -- you know, I would observe that there are a small handful of large companies that are driving the returns in the S&P 500 and private equity looking at the fund universe, there's a larger percentage of funds that are driving that turn. I do think it is an argument for having a more diversified portfolio. So taking more of a scattershot approach, where you're investing in one or two funds per year, that is going to increase the potential that you're going to underperform public markets.

MR. SIRRI: Well, let me ask you a bit of an integrated question then, before we throw it open to the panel. And I think Ed said we can go a few minutes over but not much. You all are experts in this area. You've thought about all the issues, the good, the bad, the ugly. Net, net, do you think this is a world where

retail investors would be better off if they had some form of access to these private markets, taking into account all these imperfections that you all have been talking about?

MR. JENKINS: I guess I'll start off again. So I think from a choice perspective, I think certainly having a choice. Although the challenges a lot of the panelist have alluded to, I think first is the appropriate structure. And then second, having the appropriate transparency so that retail investors can make an informed choice. So that I think those are the two limiting factors potentially for whether retail investors should have access to these investment opportunities.

MR. SIRRI: Josh? Ludovic? No?

MR. PHALIPPOU: Josh, go ahead. And I can go after.

MR. LERNER: Well, I feel there's no return to being a centrist. Otherwise I guess our governor Charlie Baker would be running away with the Presidency, the Presidential election on the Republi-crat ticket. But I do think that you know, the points that were raised of saying that -- I would think that before this could be done, you know, really addressing some of those issues about both the clarity of presentation and the

fee structures, so they weren't stacked against the retail investors, would be really important.

MR. PHALIPPOU: So the way I would say it is it took 90 years or nearly 100 years for the SEC to get a comprehensive set of regulations for the mutual fund industry in order to close all or most of the loopholes. As we went, people demonstrated that, you know, there was people who were doing fund incubation in order to address strategy calls. They showed that people do some late trading to play with 3:30 p.m. close, et cetera. And there was limited ways to do tricks with public markets. And some mutual funds went out of their way, a number of them, to find tricks, okay? And it took 100 years for the SEC to close most of them, okay?

Here the SEC hasn't even started. So if you are to do that, to allow this investment to be there alongside mutual funds and the like, then it has to be a level playing field. You need to have the same rules. You need to catch up, in a universe that is much more complicated than mutual funds to get the same rules in. The equivalent of late trading, the equivalent of incubation, et cetera, all that needs to go through. If you have all of these rules in place, there is no reason why private equity should be excluded. But holding a private asset versus public should make no difference.

It's not a problem. The problem is that you have a huge set of very advanced regulation on the one, for one type, rightly so, and the other type would require even more regulation because it has even more -- you have even more room for trickery. Then you have zero. And so that's the gap that you have to close. If that is closed, there's absolutely no problem for people having private versus public assets.

And notice that even pension funds do not even report the right fees that they are paying, particularly. So all these efforts you did on mutual funds to try to get an expense ratio, it took years to the SEC to try to say what would be a total expense ratio; what would be a fair way to present expenses of mutual funds. Here you are in a universe where it's a hundred times more complicated to come up with a total expense ratio equivalent. And pension funds are really not there. So you have a lot to do in order to let people in on a level playing field. And you will have to do it, because they should be able to invest in private assets. But right now you don't have a level playing field. It would be really weird to me that mutual funds are allowed to just be on the side of private equity and nobody plays by the same rules.

MR. SIRRI: All right. We have time maybe for a question, at most two. Russ, do you want to ask?

MR. WERMERS: Thanks, Erik. Great panel of top experts, obviously. So I think this question relates to the last question, Erik, that you posed, for the comments that your panel made, in response. If I may, given the dangers that have been pointed out in this panel, which are very useful, I think: high fees, misrepresenting returns, things like that, using inappropriate statistics, I think I'd be very reluctant at this point to myself invest in a private equity fund. But I may very well be -- I may very well be interested in investing in a Fidelity fund that invests in private equity. It's held shares in a private equity fund, or through a price mutual fund that it's attained. So what -- I guess my question is, to what degree would these concerns about private equity valuation be over in private equity as a potential asset class within the mutual fund industry?

MR. SIRRI: Any of you want to handle that?

MR. LERNER: I'll take a first shot, I guess. Which is that, you know, there has been a history of publicly traded private equity. Not so much -- you know, clearly more recently we've seen cases of management companies going public. But earlier we saw a number of examples of you know, funds of various types, you know,

doing that. In fact you can go back to the, you know, the very earliest days of the venture industry with American Research and Development and the other early venture funds, which essentially raised money from the public, not because they wanted to but simply because the endowments and others just wouldn't invest in them, because they didn't understand or appreciate what they were -- what they were doing.

I think it is fair to say that, you know, the experience of the publicly traded funds has been somewhat mixed. But how much of that is due to the fact that you know, being in a public environment when one's doing long-run private investments is hard. But there's a disconnect there. And how much of it is just due to the fact that in some sense there was a little bit of adverse selection, where maybe some of the, you know, some of the things that went public over the years were not perhaps the -- you know, not talking about the management companies, but raised funds from the public were perhaps not some of the best people who just couldn't raise money in other -- in other avenues. So I think it's a fair, fair question.

MR. SIRRI: Any other panelists want to remark?

MR. JENKINS: Yeah, I would add to Josh's

context, there is also, in certain jurisdictions, semi-liquid vehicles that allow monthly or quarterly subscriptions and redemptions. I think primarily Australia and Europe. In additional to some of those traded structures which are primarily listed on European exchanges, there are also what I would think of as more of a hedge fund type structure for some of these private investments.

MR. PHALIPPOU: Yeah, I think it's inevitable. One way or the other way would be more and more private assets. Like mutual funds would push to have more of them. Private equity funds would push. You have to face the situation. I think it's inevitable that then probably the balance would be struck to add, you give quote liquidity and assessment, and so every quarter, auction days or something like that. But we are -- we are relatively sure about this NAV, that this market NAV, that we do like an auction. And then we have then a fair redemption and trade point for people. And maybe public markets will go this way. You know, I don't think people really need to trade every millisecond, so, you know, to have like these windows where we run many auctions and then we are done.

MR. SIRRI: Well, look, you've certainly given us a lot to think about. Ed was kind enough to give us

five extra minutes, but I think we've taken our time. On behalf of the subcommittee and in fact the entire AMAC, we thank all four of the panelists. I thought it was excellent. You raised a lot of ideas. You've given us a lot to think about. So thank you for your time. And Ed, I'll turn it back to you.

MR. BERNARD: Great. Let me add my thanks. And actually quickly, before I close up this session, Rama, did you want to say anything else, or should I close us out?

MR. SUBRAMANIAM: No, go ahead Ed. Go ahead.

MR. BERNARD: Okay. Let me just echo Erik's thanks. That was a spectacular panel. We're grateful to all of you for taking the time to be with us. And you have given us a great deal to think about. As we break for lunch, I would comment that both the ESG and the private investment panel now gives us a clear sense of just how not only important but how complex the issues we as a committee have taken on. And I commend the subcommittees for providing the attention that's required to tackle complex issues. So with that, we will break for lunch. Give everybody a chance to get away from their screens. We will start again at 1:00 promptly. For those of you watching the public broadcast, you'll see a holding screen in place until about 1:00. So with that, everyone, please enjoy a little time away from the screen. And committee members, please be back a couple of minutes before 1:00, and we'll get going promptly at 1:00. Thanks very much.

(Whereupon, at luncheon recess was held from 12:21 p.m. to 1:00 p.m.)

A F T E R N O O N S E S S I O N

MR. BERNARD: Okay, welcome back, everyone, from lunch.

Just as in our July meeting, Gilbert Garcia and team have assembled a distinguished group of speakers. And I'll turn it over to Gilbert now to refresh us on the arc of the team's overall work and introduce the panel.

Gilbert?

MR. GARCIA: Thank you, Ed.

And let me just first say my own couple of thanks, if I could, which is I want to say thank you to Chairman Clayton, to all the SEC commissioners, to Dalia Blass and, again, to Mr. Ed Bernard for making this topic a priority, and for it to evolving into a subcommittee [sic].

And I want to thank my new members that are going to start working with me on this, Mr. Paul Greff and Scot Draeger, who join me.

And I want to say thank you to Robert Marchman, who in many ways has been the Obi Wan Kenobi supporting behind the scenes. He often is -- you know, doesn't get the recognition he deserves. But you know what? He's been phenomenal.

Now we have a chance to do something really profound here with AMAC, something that can address and at least move the needle some to address this alarming wealth inequality that exists in our country today. And this wealth inequality is really the root of so many of the things that we're facing today, because it really leads to unequal access to health care, to justice, to education, and to women and people of color, unequal access to really achieving the pinnacle of the American Dream.

So I'm going to review our journey here with this committee, and I'm going to talk about where we've been and where we're going. And along the way I'll give some of the formalities of what we're going to do today on the panel.

So we started last AMAC meeting with data. We heard about the role the consultant community plays in the asset management ecosystem. But we also learned about the incredible concentration of assets among the largest consultants, and their extraordinary influence

on asset flows.

But sadly, we heard from our speakers last time, we learned about the total disregard for transparency by many of these largest consultants. We learned how they blatantly ignore requests for such basic information, best practice information like employee demographic disclosure, like information on manager recommendations, and even conflicts of interest. We even heard that the SEC, when sending out their diversity assessment to the 1,300 regulated entities, the responses they received cover just 69 -- 69 out of 1,300. If that was my daughter's math exam, 69 out of 1,300, my wife and I would be alarmed, and we would immediately conclude that there's something very wrong.

But today is going to be much more uplifting, because today we're going to celebrate some of the best practices by some of the industry leaders. And I am hopeful that there are people in the universe watching and listening who will listen to some of the things that they have done, and will learn from some of the things that they have done, whether it's what they did to avoid issues, whether the issues that -- they learned bumps along the way, but, at the end of the day, to learn from them some of the best practices that they have taken

upon themselves to write a good playbook.

So we're going to have two panels. The first will consist of three consultants or consultant-like entities. They're going to each speak for 10 minutes. And then after the 10 minutes we will have 15 minutes of Q&A. After that first group we will then hear from three more speakers, some of the largest allocators, some of the leaders, again, in this area. They will all speak for 10 minutes, and then there would be 15 minutes of Q&A after those 3 speakers.

In December we hope to bring forward to the AMAC some suggestions, and we hope to bring forward some other industry leaders like John Rogers, like Martin Cabrera, people who have been working on diversity for 30 years in the financial services industry. And then somewhere in early 2021 we hope to bring concrete suggestions before the AMAC Committee for consideration. That -- ultimately, we hope many of those good ideas will go forward to the SEC themselves.

So having said that, our first panel is going to consist of Mr. Mike Manning, who is the managing partner of NEPC Consulting, one of the largest 10 in the country, and one of the leaders. The other will be Mr. Mike Miller, who is a chief investment officer of Colonial Consulting, one of the leaders in the foundation space, and he has an interesting story of how they got involved with diversity. And the last will be Mr. Clayton Jue, who's been one of the leaders in the manager of manager diversity space for over 30 years.

So, Mr. Manning, please take it away.

(Pause.)

MR. GARCIA: Mike, I think you're muted.

MR. MANNING: I'm back. You missed a great start. I'll start all over again, though.

So I want to say thank you, Gilbert, and for, you know, the entire membership of the AMAC for tackling this really important issue and helping the industry move forward on this. I'm excited to be here today, and to play my part in that conversation.

You know, NEPC is one of the largest investment consultants in the industry. And I think, because of that, we owe a responsibility to show leadership across a variety of ways, but certainly as it relates to promoting diversity. I'm proud of the work that we've done to date, but I also recognize that there's a lot of work to do in the industry broadly, but certainly also in NEPC.

So my conversation today is to talk about the three ways -- the three areas in which we're taking steps to improve diversity here at NEPC: the first of

those is dealing with our own internal workforce; the second is how we're working to develop a more inclusive culture at NEPC; and then, finally, what we're doing to engage with the diverse manager community.

So starting back on our workforce, you know, the focus here for a consulting -- in a consulting firm that preaches the benefits of diversification for our clients, in terms of their asset allocation, we think it's critical to have diversity of thought in our workplace and in the decision-making bodies at NEPC. And so we're working hard to identify people, to bring them into NEPC, and to incorporate those voices and those perspectives that are, frankly, different from a lot of those that are already here at NEPC.

I'm proud to say that we have -- 50 percent of our new hires in 2020 have been minorities. So we're really excited about the steps that we're taking there. But we also recognize that we have to do more in terms of lifting up the diverse candidates we have at NEPC, in terms of getting them to more senior positions.

One of the steps that we're taking -- and I think, if you look at the industry as a whole, there's not a lot of diverse representation in the consulting industry. And so what are the steps that we at NEPC can take to build a more diverse workforce ourselves?

I mean, one, obviously, is to look to people who may not be consultants, but are adjacent within the investment management industry, and trying to attract them into the consulting marketplace.

The second way is to build a groundspring of talent. And, you know, that is through our MBA program, through our internship program, try and identify diverse talent, bring them in, expose them to, you know, the exciting work that we get to do at NEPC, where you get to use your intellectual mind, you're engaging with clients, and doing really important work as a trusted adviser.

You know, we think we have a lot to offer to folks who want to join our industry. And so developing specific programs to target increase in the diversity -- and every one of our hiring managers has a goal that 50 percent of their team has to be diverse. And if it's not, they need to make progress towards that throughout the year. So that's one of the things that all of our managers are measured on.

Once we've got a more diverse workforce -- and we understand it's going to take a while to get there -- we want to have a place that's inclusive. And the steps that we're doing to do that are multifaceted. A few recent things are we've had unconscious bias training

for the senior leaders at the firm, and are going to cascade that down further. It's leading into the conversations, you know, from the events this summer with George Floyd, and just talking about social and racial injustice more broadly across the firm, and then also creating some affinity groups within some of our diverse communities so that they can work together to help us understand what we need to do to be a better environment, in terms of are there programs that we can put forward, are there ways that we can do a better job of mentoring or developing that level of talent.

You know, our ultimate goal is for the people that we're able to bring in to NEPC, to allow them to be their full and best self at work. And to the extent that we can do that across our entire workforce, you know, we think we'll be better off as an organization, and from that our clients will benefit from that, as well.

So those are the two internal aspects: building a more diverse workforce, and then making it more inclusive. The third area I want to talk about is what we're doing in terms of engaging with the investment manager community. And here it's really a three-step process.

The first step in that process is making sure that we're canvassing the full landscape and engaging with diverse managers. And it's not -- it is easy sometimes for diverse managers, particularly those that are smaller, to have the same level of marketing team or marketing staff to go out and reach out to all the consultants. And so, for us, one of the things that we're doing is we have a goal that our number of manager meetings will go up 10 percent by year over year, in terms of the meetings that we're having with diverse managers.

So by expecting and demanding all of our researchers increase their level of exposure to the managers, we hope to get to our second goal, which is that we want 10 percent of our focused placement list, or one-rated strategies, to be diverse managers by the end of 2021.

So when we started this, we were at six percent. We have moved up to seven. We clearly have work to go. But what we want to do is not just canvass the landscape, but we also want to make sure, from that canvassing, we're identifying and profiling the best managers that can then be brought out to our clients to make sure that they are getting exposure to them through the manager search and identification process.

The final one of those, where we're holding

ourselves accountable, is for our internal profit sharing plan, and for those assets that we control in discretionary mandates. We're measuring the percentage of assets that are actually hired by diverse managers. So we want to make sure -- and that we have looked at it -- our exposure is we've got about twice as much in assets as our broad -- advisory client base that are held by or managed by diverse managers.

So, again, really, a three-pronged approach there: one, making sure we're canvassing the landscape; two, that we are identifying managers and rating them highly, so we're giving them to clients as recommended managers; and then finally, where we control the assets, that we're putting our money where our mouth is, and building a portfolio that contains assets managed by diverse managers.

And then, Gilbert, to your point about transparency, you know, I think that's where we've tried to lead in being transparent. And sometimes the numbers -- I know the numbers aren't always where we want to be. But in -- you know, when clients ask, or when industry experts ask, we give them full transparency in terms of who works at NEPC, you know, what levels they are, you know, in terms of ownership or senior professionals, you know, all the way down to entry level. We think it's

important to share that and be a leader in that transparency, and would actually love to see more of that coming back from the manager community, because it allows us to understand who is doing a great job on that front.

So with that, I'll stop my comments and look forward to your questions.

MR. GARCIA: Mr. Manning, we salute you.

Mr. Miller?

MR. MILLER: Good afternoon, everyone, and thank you. I want to thank Chairman Clayton, the commissioners, SEC staff, Ed Bernard, Gilbert, of course, and the AMAC for focusing on this critical topic. My name is Michael Miller, and I'm the chief investment officer of Colonial Consulting.

We are a New York City-based investment adviser whose predecessor found -- firm was founded in 1980. I joined the firm in 1986, so I have spent many, many years in this industry. We count approximately 120 endowments and foundations as clients today, and they have capital of approximately $35 billion.

So, as this section of today's meeting is focused on advisors and allocators such as our firm, I want to briefly share our story with the hope that it will provide the Commission, staff, and this committee

with ideas regarding how the SEC might use its authority to inspire meaningful change.

I want to begin by emphasizing two points. First, as you heard at the committee's last meeting, a meaningful and lasting shift towards an equitable, merit-based distribution of capital across the institutional investment industry is a very long road. We've been at this for nearly eight years now. And while there is much we can point to -- and I'll describe momentarily -- regarding the positive impact this has had on our client portfolios, it's very clear to me that there is very, very much to be done. And we seek to ensure that our process and team are objectively and aggressively pursuing exceptional managers that are majority-owned by women and people of color.

Second, until the value of having diversity across the portfolio of decision-makers is as natural and widely accepted as concepts such as asset class, diversification, style diversification, et cetera, we will never get past conversations around social engineering or the idea, misguided as it may be, that allocating capital to diverse managers is somehow at odds with investment success. I cannot overemphasize the fact that, in reality, the opposite is the case.

Back to our story for a moment. About eight years ago, one client came to us and asked us about the diversity of their portfolio, the degree to which our research process was providing them with a level playing field, or providing a level playing field for the investment manager community. That began a journey which started off very slowly, as we assumed our work was actually far better than it actually was.

Lesson one for us in this was the power of impression over facts. And until we actually sat down and measured our work, we were truly unaware of how poorly we were doing. Even after realizing there was a real issue, this was still just one client's request. Change can be difficult and costly, and absent significant pressure, our efforts, no matter how well-intentioned, were gradual.

We also had very little appreciation for the fact that there was much more going on here than just the perpetuation of a system that definitively excludes women and people of color.

Fortunately, we have a talented and diverse leadership team and staff that caused us to get more serious about manager diversity somewhat internally. Our effort began to accelerate almost four years ago, and has produced the following results.

Colonial's advisory and discretionary client base

has 8.4 percent of its assets today allocated to diverse managers, and 12.6 percent of it allocated to managers that are diverse around the world.

Our discretionary or outsourced CIO client portfolios have just under 22 percent of their assets allocated to diverse managers globally, on average. This difference between advisory and discretionary is due to the fact that our discretionary work is relatively new. So we built portfolios more recently from a much more robust and diverse research effort. Ninety-two percent of our clients use at least one diverse manager, and there are currently forty-seven such firms across client portfolios, with forty of those forty-seven being domiciled in the United States.

That line-up I just referred to -- refers to is, essentially, across all asset classes.

I also want to categorically state that we're still missing out on a great deal of talent, and are roughly, in my view, in the third inning of this effort, both in terms of the number of firms we recommend, and, even more significantly, the capital that has been invested.

With that said, we're not unhappy with where we are, and I would point to three major items that helped us get here.

One is a sustained commitment on the part of the firm's leadership to this work. That involves several items that were all done simultaneously: first we hired an exceptionally talented individual to be 100 percent dedicated to ensuring that diverse managers were an integral part of our research effort; second, we have been multi-year sponsors of a significant number of trade organizations that promote and support diverse managers, and seek to improve the future of the talent pipeline; third, we made it very clear to our team that finding world-class, diverse managers was mission critical in terms of our ability to most wisely advise our clients.

The next major issue was to recognize that hierarchical or centralized decision-making in our research process could introduce a lot of issues that would slow or stop the approval of talented, diverse managers during a period where individuals on our team were each on their own journey towards becoming less biased in their work. By changing the way we decided on managers and the way we structured the vetting process, we were able to overcome some of those hurdles more rapidly.

Third, we've long been big believers in recommending newer firms, younger investment

professionals, and this naturally allowed us to avoid the very real problem of trying to find a significant number of well-established and large diverse firms, as there are very few such choices. And that's, obviously, one of the reasons this committee and Commission is focused on this issue currently.

So in thinking about how the industry moves forward, I have just a few comments.

First, particularly in the early days of our effort, we struggled with the question of whether and how we should raise this issue with clients. At the end of the day, we simply allowed the quality of the managers to do the talking. This was convenient, but -- and allowed differentiated excellence to do the talking for us, but it also avoided the bigger picture issue that was at work.

One place where a lot of progress can be made is to make this into a business issue for the advisory community. The more firms like ours hear from clients, hear from the Commission, then the more quickly we will all act. Remember that we were able to move very slowly in the beginning because we felt no pressure to make change, other than the fact that we just wanted to. And that's not good enough.

Our suggestion for the Commissions [sic] are to begin by continuing to hold hearings such as this one, and to raise the profile of the industry's lack of diversity. The second is to somehow mandate disclosure of each adviser's client assets in the hands of diverse managers. This should not be optional, and it will not come as a surprise to hear that, when we were asked to commit to annual reporting to our clients, who are interested, we did not want to embarrass ourselves, and it was quite motivating.

The reporting we developed includes the number of diverse managers we meet each year, the percentage that represents of all manager meetings. We also report on the number of diverse managers that we are currently recommending, the number that our clients currently employ, and the dollars that our clients have allocated to diverse managers. These are not complex items to track, and the SEC and asset owners demanding ongoing disclosure would have a very significant impact.

The other major item to consider is the definition of diversity. Ours is more than 50 percent ownership, and this represents a clear and important line in the sand. That is not to diminish the efforts of firms that have strong diversity amongst their ranks, and are clearly making meaningful contributions to this issue. However, reporting must be based on consistent,

objective standards, and majority ownership is a very, very good place to start.

Finally, the urgency to take meaningful steps forward involves an important duality. For many it begins with a desire to improve equity in our society. At the same time we must also expand the appreciation for the fact that manager diversity is about producing superior outcomes.

This was the aha moment for us, as we started to meet with more diverse managers, and realized that this was a huge win-win situation. We were finding differentiated talent, and unique talent that was being overlooked or ignored, and this is where we became extremely enthusiastic. Not only would our clients be able to leverage their capital to take on an equity, but their portfolios would be more wisely invested due to the clear and obvious benefits of differentiated thinking.

As you look forward to your efforts, I'm excited to see and looking forward to seeing the continual and well-documented progress towards a more equitable and superior investment community.

I thank you again for listening to me, and I appreciate the invitation to be here today.

MR. GARCIA: Mr. Miller, thank you. I'm

giving you a high five over the screen. I hope that you saw that.

Mr. Clayton Jue, you're up, sir.

MR. JUE: All right, thank you for having me here today, Gilbert and committee members. I'm Clayton Jue. I am founder and CEO of Leading Edge Investment Advisors. Now, we are manager managers founded in 2005, and we focus on creating and designing emerging manager programs for institutional investors.

I've been in the manager of managers business, specifically focused on emerging firms, since 1990. Prior to that I was with a major consulting firm. So I have quite a bit of experience looking at the challenges and finding solutions, different solutions on how to address those challenges.

I want to highlight that we are -- I am similar, as a manager of managers, to some of my co-panelists here who are consultants, but I'm also different. I'm similar in the respect that we act as a fiduciary for our clients. I'm different in the respect that I am a comprehensive provider for an emerging manager program.

What does that mean? That means I go out and I actively source and identify managers that -- similar to your consultants. So we do go out, and we do

evaluate the product offerings that they have. We look at their competitive strengths. We look at their capabilities. And, basically, we try to determine what they're good at.

Secondly, I -- after finding out what they're good at, I design and construct an investment program that utilizes the individual strengths and capabilities of the managers. We also determine who the managers are, the allocations, and the role they play in the investment program.

And then thirdly, we evaluate and provide ongoing oversight of the program, making changes as necessary, as well as providing support and guidance to the underlying managers as they grow their businesses.

So in my capacity as a manager of managers, I am a talent scout, I am a casting director, and I am also a team coach. So that's a little bit different than most general consultants.

Our clients typically give us full discretion to implement the program. However, I like to point out that it is a collaborative effort, and we work closely with all of our clients on all the decisions.

My comments today are based on my 30 years of experience, observations, and reflections as a manager of managers.

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The first principle I think that is important for maximizing program success is to make diversity and inclusion a full-time effort, as opposed to a part-time activity. Many institutions assign this responsibility or this activity to an existing staff member who also has many other responsibilities. And that's really not sufficient, because the emerging manager universe is quite broad, and it requires a wide bandwidth to cover that universe.

Just as an example, the SEC has -- or had, at least in 2019 -- approximately 12,900 RIAs. That's a lot of firms. Most consultants will only focus on the largest firms, and they have all the assets, or most of -- the majority of the assets, as we all know. So to actually cover the universe adequately, you've got to have bandwidth.

Secondly, you've got to have expertise at looking at smaller firms. So this is a little bit of a specialized capability. You're looking at smaller firms, they have a limited history and limited track records. And you have to have the expertise to be able to look at that closely and to make judgments and interpretations and decisions based on that. This requires resources.

So how does -- how do institutions do this?

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Well, they can assign a staff member to be dedicated full-time to doing this, and give that staff member adequate resources. Or they could hire firms such as ours, a manager of managers who specializes in this area. Many of our clients do both, so there is not one only right approach.

The second principle I'd like to focus on is that the emerging manager program should be fairly flexible, so a cookie-cutter approach does not work for everybody. It must be flexible. A customized approach allows the program to utilize the separate strengths of each of the individual firms. It is able to adapt and change as the market and conditions dictate. Manager selection and allocation should not be constrained by arbitrary AUM or track record requirements; it should focus on a manager's true operating capability and capacity.

The biggest challenge for emerging firms today is getting that first account, and there are just many policies against being the first account for a firm. So our programs try to overcome that.

And being able to adapt, the program should be able to move to areas to where managers are successful. So, for example, in the last few years many of our programs migrate from domestic equities, which has been

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very challenging for active management, I think everyone is aware of that, that is changing back the other way more recently, but many of our programs did migrate to the international equity markets, and managers have been very successful in that area. So being able to adapt, being flexible, that's also very important.

The third point I want to point out is -- for success is long-term commitment. There is a couple of do-nots here.

Do not become discouraged if the initial results are not -- are disappointing. You really just have to be persistent, you have to be committed.

Another do not is you do not allow the program to be viewed as a static, set-aside allocation. This is sometimes viewed as a compromise in standard and/or performance. That really doesn't help. The program should be able to grow. A static program sometimes creates tension between different diverse groups who are pitted against each other for those allocations. So to be able to solve that, the program should grow and expand, and provide more opportunity for everyone.

Lastly, I would like to reiterate the twin requirements of transparency and accountability. It's really important. The latter, accountability, should be very granular.

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So in closing, my comments are not new. My concepts are not new. But, like in anything else that is done well, the devil is in the details.

Thank you.

MR. GARCIA: Thank you, Clayton. Thank you very much.

We are on time. Why don't we see if we have any questions out there. Any questions for any of the speakers?

And I'll certainly lead off with one, which is, Mike Miller and Mike Manning, do you all have someone dedicated, as Clayton said, full-time to sort of working with emerging firms and minority-owned firms and women-owned firms?

I'll start with you, Mr. Miller.

MR. MILLER: Yes, we do, Gilbert. We have someone who has become a bit of a legend in this industry, Angela Matheny, who is head of diverse manager equity at Colonial, and she was actually recently promoted to be the chief of the investment staff, working with me to run the entire team.

But I want to be clear, she's a point of contact for diverse managers, but every member of our team has engaged a diverse manager, and Angela is the source here, in some degree, although that's moved almost beyond her at this point. And she's the cheerleader. She's actually the one who, I will tell you, is the enforcer in the firm to ensure that we all stay on track, and that we don't lose any of these managers, or our diverse managers, in particular, in the flood of ideas that come our way. So that's an incredibly important part of what we're doing.

MR. GARCIA: Mr. Manning?

MR. MANNING: Sure. So we do not have a dedicated person. Our approach has been that each person who is managing a particular coverage area, you know, whether that is international equity, corporate income, anything along those lines, they need to know their space exceptionally well.

You know, we've seen other models where it is one person off to the side meeting diverse managers -- and it doesn't sound like that's what's going on at Colonial, so I'm not -- no aspersions there. But, you know, if that person is doing -- to me, that's not -- it is not fully involved in the research process, and it is seen as something separate. And from my perspective, I think we should look at these managers -- and I think Mike Miller's comments were great about, you know, one of -- the rationale on this is you're going to get great managers out of it. So we want our dedicated

researchers to look at that. And so that's the approach that we've taken.

MR. GARCIA: Thank you. Michelle, I know you had your hand up.

MS. BECK: Yeah, I -- you know, I heard some comments about, you know, focusing on where ownership structures are minority and female. And I do wonder where it leaves all of the companies where -- that are publicly owned, or that have significant diversity in their management structure, but not necessarily the ownership structure.

So I did want to understand how do you incorporate them, particularly in the world where so many assets have gone to passive, which tends to favor large-scale, very big companies. So does that not matter, should we not be looking at that?

What would it do to the statistics that we heard about in the first meeting if we actually expanded the envelope a little, and looked at larger asset managers and their diverse populations?

So I am curious about your thoughts.

MR. MILLER: Well, I would be happy to start. Is that okay?

MR. GARCIA: Yes, thank you, Mr. Miller.

MR. MILLER: Yeah, so that's a really

important point. And I will tell you this. So we are -- when I said before that we are defining diversity this very specific way, we're -- that's important to us, because there's a lot of ways that you can massage the numbers -- which is not what you're suggesting, I realize -- if you don't have a definitive area of focus that way.

But with that said, and when we -- when I referred to differentiated thinking, now we're talking about some of the things that Mike Manning brought up before, too, which is, you know, what is the leadership structure, the diversity, and who are the decision-makers, specifically within large organizations and the large, publicly-traded asset managers.

So we don't include them in our statistics, but we very-much include them in our portfolios, because that's how we press this advantage even further.

MR. GARCIA: Thank you. Mr. Manning, did you have a comment there?

MR. MANNING: Absolutely. So, you know, I guess one of the things -- and the corollary here might be the way that NEPC approaches ESG. And so, you know, there, when we evaluate managers, we evaluate them on their commitment to getting better. You don't have the

same objective metrics that you do that Mike Miller talked -- sorry, we have two Mike Ms, it's a little harder -- that Mike Miller talked about on the clear demarcation point of 50 percent ownership or not.

I can see us at some point evolving to a rating on diversity which includes not just the ownership, but the leadership, and then also the steps that they're taking as an organization to promote diversity.

So, you know, I think it's, you know, admirable for an organization that is still majority owned, but taking meaningful steps to promote that diversity. It's just that it's not an objective measure in today's environment, and I think we're still working to -- at a minimum, we would like to get the objective measures and the transparency to start there. But, you know, we're continuing to ask about what they're doing to promote a more diverse population, not for the sake of diversity, but for the sake of you get better decision-making if you've got greater thoughts around the table.

MR. GARCIA: Clayton, did you want to weigh in real quick, before we turn it over to Mr. Bernard for a question?

MR. JUE: Well, diversity in larger public

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organizations, actually, is very important. One of the reasons why many minorities and women went out on their own earlier -- in earlier years was because they were frustrated with their advancement within these larger corporations. So definitely, they should be recognized for their contributions. They should be rewarded for that. They should be able to advance based on that.

I'll tell you that many of the large organizations are very proactive about their diversity efforts. We really appreciate that. And we have a good network through them, as well. We are able to find managers of -- minority individuals or women individuals who want to go out on their own very early on from these organizations, and that is part of our active sourcing.

MR. GARCIA: Thank you.

Mr. Bernard?

MR. BERNARD: Yeah, a question, if I could. I know in our next group we've got three asset owners, and we're delighted to have them to talk about this, but you all serve a wide array of clients who are asset owners, and I'm curious to hear your thoughts on the state of play, and the extent to which asset owners are asking you to find diverse managers, or you're telling them they need to ask you.

You know, to what extent are you having to

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persuade them, and to what extent are you seeing increasing receptivity and/or demand for that?

MR. MANNING: I'm happy to start. Mike Manning again.

So we work across a whole array of clients. We are probably the most diverse institutional consulting firm, by the type of clients that we service, and it really is across the board. You know, I think if you look at -- particularly in -- at a lot of the large public funds, they may have specific mandates, whether it be to hire someone like Clayton's firm, or they have their own internal team, where they're directing -- or, you know, an objective for them is to have a certain percentage of the assets or the fees -- and I think we should -- it's important, is not just about the assets, it's about the total fee dollars that are being spent to managers -- there are some that have those specific carve-out programs, you know, like Mike Miller and his firm.

We have endowments and foundations that are more socially minded, and that's an important aspect to what -- and families, actually, that -- that's a really important goal for them, and they want to -- they are asking us and pushing us, I guess, in the same way that Mike talked about, whereas there's a subset of managers

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-- or clients excuse me -- where it may not be that important.

I think one of the areas, interestingly, with the DOL recently, you know, in their conversation about ESG, you know, is this a factor that an ERISA fiduciary can take into consideration when they're building a portfolio? You know, and some of the recent discussions about where ESG is not something that should be factored in for some portfolios, you know, I think is a little bit concerning.

But that is -- I would say we're all over the board, in terms of where clients are. There are some that are very forward-looking, and are pressing, and want to have a dedicated mandate, and there are some who either, frankly, don't care, and their focus is on just, "Give me the best managers," or worry that having that as a mandate might not allow them to meet their ERISA duty. So --

MR. GARCIA: Mr. Miller, do you want to comment on state of play?

MR. MILLER: Yes, sure. I'd be happy to. So it's interesting. Up until this year, I'd say the state of play was there were two things. One is very few people asked us about it.

But what was interesting is, when we started

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to raise the issue not in general terms, but with specific manager ideas, I was actually quite, I must admit, surprised at how receptive clients were. It was almost like they were waiting for us to come and say, "This is how you should do this," and they embraced it quite broadly. It was really, really interesting to me, and kind of made me wonder what took us so long.

This year things have changed. A lot more clients are asking about diversity in their portfolios. They see it as another tool they could use, in terms of some of society's ills that Gilbert described earlier. And we're seeing a much larger level of interest in the subject in general, which is heartening.

I just want to clarify one thing. We don't have separate sleeves, and I don't think anyone implied we do, but I want to make it clear. Diverse managers are part of our portfolios. And when they get to 30 to 50 percent of the portfolios, we'll feel like we might have achieved something worth achieving. But there is no sleeve for diverse managers. There's no carve-out for them. They are managers in our portfolio, generating excellence for our clients alongside our other managers. That's the idea.

But yeah, that -- so the state of play is improving it. But I will say it's not -- I wouldn't call it a tsunami, by any means. It's just slowly but surely getting better.

MR. GARCIA: And Mr. Clayton Jue, I'm going to phrase a question just a little bit different. Given some of the things that have recently happened that we've read about in the manager of managers space, what is the state of play for you now? Are things changing? Are you seeing more activity?

MR. JUE: Certainly seeing a lot more inquiry on the topic. We've had a number of clients that have been committed to this area for a number of years, and we're really proud to have those clients.

A lot of the inquiry -- there are new inquiries, really, from organizations or institutions that -- they either haven't tried a -- you know, a focused effort in diversity and inclusion, or they have tried it before, but the people who were in charge of that have moved on, and there is no institutional memory in place to what has been done. So then we get organizations come back to us, and they start all over again from scratch.

Now, this is a problem with a lot of public funds. Staff turns over and people leave. But you've got to have a record of what's been done, what's been tried. And we're getting a lot of questions on, you

know, what's been done in the past, what's tried, what's been successful, what's not been successful. So that's a lot of the inquiry.

And, you know, I think that, you know, if we can have a more consistent, persistent effort, you make more progress.

MR. GARCIA: Thank you. We have about another minute or two. Are there any other questions from any of the committee members?

Well, then, I'm just going to do one more, if I could.

Mike Manning, NEPC tends to have a reputation for having one of the highest number of people of color in consultants, and research, and even a member of your board. How did you get there? And was there a decision that said, "We just need to do this," or did it just happen naturally?

MR. MANNING: You know, I can't go back and point to a specific decision, but I do know, where we have identified talent, we've said -- you know, a few people, you know, were coming into the organization and, you know, didn't have a spot, you know, came up and said, "Hey, she's incredibly talented. Let's bring her in, and we can find a place for her," you know.

And then, you know, with Sam Austin, who

recently joined and is now a part of our internal board, when we did a search for someone on the West Coast, we specifically were trying to look for diversity. And so, you know, we made that a big part of -- more recently, in the last four or five years, we made that a big part of all of our searches, is trying to make sure we're interviewing a diverse slate of candidates, as opposed to just the candidates who might apply. So we're really going out and trying to canvass the world, looking for people of diversity.

MR. GARCIA: Thank you.

Mr. Bernard, I think we're ready to move to the next group. Very good.

And for our first panelists, you're welcome to please stay and be part of the conversation. But if you're busy, we understand.

So our next grouping is now going to be asset allocators. And we, again, have three leaders in this area.

We're going to start with Cheryl Alston, who is the executive director and CIO of the Dallas Employees. But she also is on many other boards. And I think you could say, wherever she goes, she touches the finger, or the hand of diversity comes. And I think that's phenomenal.

And then we're going to have Mr. A.J. Hernandez, who is the director of emerging managers at the New York State Common Fund. And A.J. is interesting because he was there, he kind of left, and he's come back. And I think he's come back, you'll see, with renewed enthusiasm for progress.

And then we're going to close with Mr. Michael Frerichs, the Illinois State treasurer. And I think you'll see why, when you hear his comments, because not only has he done extraordinary things for the State of Illinois, but he's also done extraordinary things in the area of diversity, which I think is a good example that they're not mutually exclusive, to do an excellent job and to achieve a lot of progress with diversity.

So having said that, Cheryl Alston, welcome.

(Pause.)

MR. GARCIA: I think you're muted there, Cheryl.

(Pause.)

MR. GARCIA: You want to try again, Cheryl?

MS. ALSTON: I do.

MR. GARCIA: Okay, there we go. We got you.

MS. ALSTON: Can you hear me? Yes?

VOICE: Yep, go for it.

MR. GARCIA: Yes, we got you.

MS. ALSTON: All right. Good afternoon, and I would like to express my thanks to the SEC team, Dalia Blass, Ed Bernard, committee chairman, Gilbert Garcia, and the members of AMAC for inviting me to participate on this panel. My name is Cheryl D. Alston, and I am the executive director and chief investment officer of an employees retirement fund of the City of Dallas.

The Dallas Employees' Retirement Fund is a $3.6 billion defined benefit plan for the civilian employees of the City of Dallas.

The Asset Management Advisory Committee has asked for the following, you know, very strategic -- key strategic questions: What can we do to improve DEI in the industry itself, and have all segments of society have access to opportunities to succeed?

There is a saying that a journey begins with a plan, developing a roadmap, and the courage to get to the destination. I was appointed to this position in 2004, and I have served in the role of an asset allocator for 16 years. My discussion will focus on our journey with both large and small asset management firms on the way to improve diversity, equity, and inclusion. I want to talk about why we started on the journey, the best practices, and the lessons we learned along the way, and the results. And I will wrap up with my list

of recommendations.

So first, why do we lean into diversity, equity, and inclusion? I know the committee has heard about all the statistics about diversity from the studies, but I will just focus on one statistic from the Knight Foundation report: the fact that across all four asset classes, mutual funds, hedge funds, private equity and real estate, diverse funds only represent 1.3 percent of the total assets under management for those asset classes.

After the great recession in 2008, my opinion is that progress stalled and took a step back in diversity. Institutional investors were hiring primarily very large firms. I became very concerned about the future of competition in the asset management industry if all investment services became consolidated in the hands of a few trillion-dollar companies. Diverse firms who had similar or higher investment performance for the same time period were not even given the opportunity to compete for the business, due to minimum qualifications that excluded them.

So if you asked someone the following questions: do you support small businesses; do you support innovation and entrepreneurship; do you support the creation of more jobs; do you support competition in

the market; and do you think small firms should have an opportunity to compete for business, most answers are overwhelmingly yes. Many of the inspirational American stories were built on the little guy or gal, or small, hardworking, talented firms winning against the large ones.

But if you ask someone, "Do you support minority women-owned firms having an opportunity to compete for business," the tone often changes. Why?

At Dallas ERF, our answer was yes to both questions. We support minority and women-owned businesses, entrepreneurship, and job creation. If you allocate $100 million to a large firm, it barely creates a ripple, and is absorbed by their current operations. But if you give $100 million to a diverse firm, it creates jobs.

So what did we do? We have a two-pronged approach. First, we actively engaged with majority-owned firms about the discussion on DEI. We asked for diversity statistics in our RFPs, so it should be encouraging for you to know that asset managers are completing these diversity scorecards. We wanted data on the diversity of the entire firm, and the diversity of the investment management team. And we are not the first investor to ask for this information, because we

revised the template that we received from the State of Connecticut.

When we conduct our due diligence meetings, we talk about the diversity inclusion with the CEO and president of the firm, because we do believe the tone begins at the top. Over the past 16 years the conversations have moved from awkward and uncomfortable to discussion on policies and metrics. The most sophisticated asset managers are ready for the discussion.

One highlight story was a woman approached me after a conference. She works for a hedge fund, and she told me that in my -- in the client notes associated with me they had put that I will ask about diversity, equity, and inclusion, and then about the discussion with the founder. And it was so very heartwarming to me. She told me that she felt that the reason why she had the opportunity to have this position was because I simply asked the question about what was their data, and what was their plan to improve it.

Second, for minority and women-owned firms, we started the Next Generation manager program almost 10 years ago. The goal of the program is the identification and selection of high-performing diverse firms. We were very intentional about the name of the

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firm being "Next Generation," and not "Emerging Managers," because we wanted to find the next set of firms that could grow into industry.

So what are the key points of the program?

First, governance. Everything starts with governance and the tone from the top. I report to a board that is 57 percent diverse. My staff is over 60 percent diverse. The board believes in their fiduciary duty, and they believe in a fair and equitable market.

The board included the program in their governing documents, specifically in our investment policy statement, so it lives on past the current board and past the current executive director. It should also be included in the strategic plan and the compensation plan that flows down to the entire investment team. The monitoring objectives, it needs to be done and completed by the full board, just as in any strategic plan review.

Now, there are two approaches to staff implementation. Some organizations have a single champion who is responsible for the diversity effort, and they give them a portion of the portfolio to allocate. Another approach, which we use, is to weave diversity into the DNA of all the investment team. As the companies have stated, that risk management is the responsibility of all employees, DEI is the

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responsibility of the entire staff, so that they develop the muscle and gain the expertise to make decisions long-term, and it becomes part of the DNA of the organization.

In terms of another point is a definition of diversity. We believe in the Knight Foundation definition, which is 25 to 49 percent of -- or more ownership that's represented in their study is more realistic than 51 percent, because -- and simply because of the amount of capital it takes to form a new asset management firm today. It's hard for one -- a few people to put up that additional money. So we believe 25 to 45 percent, in that range, is appropriate.

Another key point is transparency. In order to improve transparency, we started having an open house. In our office we would host an open house to talk about the fund, our asset allocation, the general RFP process, and selection process at no cost. It gives asset management firms an opportunity to ask questions. And in this COVID environment we will have to host these open houses virtually.

The next component is access. We are a public entity, so we follow the RFP process published on our website, and all firms are eligible to apply. I know there are some institutional investors that may not

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follow this process, but rely on a preferred vendor list from consultants which often may not include diverse firms.

Another component is we do not cap on asset size. We look at the size of the manager relative to the peers in the asset class. A $10 billion company in small cap would be huge, but a $10 billion company in fixed income is tiny. So you need to look at the minimum qualifications that are appropriate for that asset class.

Another key component is are there any other barriers that are not related to investment factors that prevent women and minority firms to compete? For example, one organization had an insurance requirement buried in the RFP that was so high only a very large firm could meet the requirement.

And the final component is incorporation into the portfolio. Once the firm is hired, we incorporate the firm into the overall portfolio. There is a reason we do not have a smaller pool, or graduation process into the larger pool, because we want to avoid associating diverse firms together.

I had one CFO tell me that she hired 2 minority firms over 10 years ago, and it did not work out. I asked her, "How many firms, majority-owned

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firms, have you hired in the same time period that you have terminated?" And it was five times the number. But it did not stop her from hiring another majority-owned firm.

It also gives people a reason to give them a lower allocation. I believe a firm allocation that is a percentage of the portfolio is appropriate, so the firm can grow as the total fund goes.

Just -- I just want to hit on some common misconceptions before I close. A common misconception: diverse firms cost more. No, their fees are in the range for active managers in the asset class.

Another common misconception is you need special staff, or more staff to hire diverse managers. No, a majority-owned fixed income manager and a minority or women-owned fixed income manager have the same components.

Another misconception: performance is lower for diverse firms. The Knight Foundation provides statistics to dispute that issue. And just for myself, a recent article in The Dallas Morning News listed the Dallas CRF as the second-highest performing public fund for the 10-year period. And through that entire 10-year period we have had women and minority firms play a meaningful role in the portfolio.

And the last one: diverse firms are hard to find. And what I've told my peers is I believe that a CEO who can find a private equity deal in Latin America and Asia can find a minority or women-owned firm in the U.S.

So to conclude, my recommendations: I reviewed the SEC's strategic plan for diversity inclusion for 2020 to 2022, so I'm going to tie my recommendations to some of your language.

One is to create and implement a communications strategy that further elevates diversity and inclusion as a key strategic priority, and reinforce a leadership commitment. The SEC has taken the first step with the formation of this committee. So I would encourage you to develop a formal communication plan to provide guidance on this issue for your members.

The second one is transparency. Your language says, "raise awareness by including information about diversity inclusion on the SEC's external website, and maintaining a diversity dashboard." Although I think you are referring to your own employees, providing guidance on a diversity scorecard, adopting a scorecard for your members, is appropriate, because whatever is measured is managed.

And the final is using quantitative and

qualitative data to evaluate programs and processes and identify barriers that may deter inclusivity and opportunity. And I think what you realize is that data provides a foundation for meaningful discussion. I believe in the intelligence of the boards that manage these funds and the senior teams to adopt policies and procedures, and hopefully develop new best practices for the industry.

So, in summary, just what is the North Star? In my opinion, the North Star is a fair and equitable market that all segments of American society can compete. I think this is a first step, and I want to thank you so much for your time.

MR. GARCIA: Cheryl, thank you. I'm giving you two thumbs up.

I'm not going to call on Mr. Hernandez, A.J. Hernandez.

MR. HERNANDEZ: Good afternoon. Thank you, Gilbert.

Mr. Chairman, Commission, the Commission staff, committee members, ladies and gentlemen, my name is Anyori "A.J." Hernandez, and I am the director of the emerging manager program at New York State Common Retirement Fund.

First, I applaud the SEC Asset Management

Advisory Committee for focusing on diversity and inclusion as a top priority. And I thank you for including me and my organization to provide our perspective.

You will find, when it comes to diversity inclusion, there is much to learn, much to discuss, and much to do.

Second, I would like to give a little background on my organization and the employees, beneficiaries, and retirees it represents in order to provide you with perspective on my comments and recommendations to the committee today.

New York State Common Retirement Fund is the third-largest pension plan. We have a little bit over a million. We have a little bit over a million employees, retirees, and beneficiaries. We are approximately $220 billion assets under management.

The emerging manager program is a separate platform and initiative at New York State, managing approximately $7 billion across 125 underlying managers, with 8 program partners covering all asset classes. That includes equity, global equities, real estate, real assets, credit, and fixed income.

Historically, we've always recognized the importance of this platform. But now, more than ever,

given current events, the emerging manager program has never been more relevant than it is today. Diversity has always been part of our fabric. It has always been part of our DNA. It certainly has been a part of my DNA.

Thinking about current events, the unrest, the instability that has gripped the country over the past few months has only highlighted how thoughtful we have to be in expanding our commitment to diversity and inclusion, and to the emerging manager community at large.

We have not stopped investing. We continue to increase the availability of capital and to accelerate diverse leadership and management in our emerging manager and core portfolio.

When I think what has made our program successful, and lessons that folks can take away, there are two stand-outs.

The first, which has been mentioned a couple of times here today, is tone at the top. That makes all the difference. The support that I receive from the CIO and the controller gives me the confidence to execute my strategies.

And two, having a dedicated emerging manager -- dedicated team for the program.

This team is responsible and held accountable for the successes and execution of the emerging manager program.

Some of the lessons learned, if you're running an emerging manager program, and have consultants and advisors that act as an extension of your staff, make sure they truly understand how to underwrite for newer and smaller managers. It makes all the difference between having a successful performing program, and one that, uh, will underperform.

And two, truly understand the diversity throughout the organization you work with. Understand the gender diversity, ethnic diversity, diversity in leadership position, diversity in workforce, just to name a few. Get the whole picture. It is my philosophy than an asset manager, or any organization for that matter, is at risk if it does not have a diverse and inclusive culture.

Which brings me to my recommendation. As you know, the topic of diversity and inclusivity is multi-faceted, and there's much to consider and much to learn, and I would say that seldom there is one -- there is one solution for such a complex problem. So, I offer the following suggestion, and ask you to reflect on them in addition to any policy changes that are needed, uh,

transparency, uh, that is crucial, uh, engagement, which you have been doing thus far, and accountability, which we all expect.

Um, I have two specific recommendation where the SEC can take immediate action -- sort of the low hanging fruit, if you will. One, increase diversity in personnel within the SEC, particular in decision making position.

Today, the lack of diversity is the enemy of our organization as we saw earlier this year, particularly in government where there is so many important decisions being made for the country, we want to see the face of America in our civil service workforce, diversity not only on race and gender and ethnicity, but also people of different views and experiences, how a person approaches a challenge, how a person solves problems, and how a person sees the world. In my opinion, diversity prevents groupthink. It helps us understand and learn multiple viewpoints, it helps us grow, and it benefits everyone.

Your website indicates that the SEC is more than a workplace. It's united by a core set of values, and is a career with conscience. SEC staff members play a critical role protecting investors, making markets fair and efficient, and helping companies grow.

Continue with what you're doing with this outreach. We are here to help

And this brings me to my second recommendation. Similar to what we are doing on an annual basis here at New York State Common, include diversity in the SEC audits, particularly diversity at the top echelons of funds and businesses. This is a subtle yet powerful message. It sends a tremendous message that the SEC is cognizant of the value add of diverse teams in businesses. At a minimum, diversity prevents groupthink.

Eventually you can develop a comprehensive metric system that measures diversity at every level, from the most junior staff to the senior leaders and from owners. This is a way to add continued transparency to diversity and inclusion by businesses.

I hope my message is clear. The lack of women and minority representation represents a risk, because it effectively creates an abyss, and we just witnessed what happens when inequality reaches a breaking point and social unrest is unearthed. Let's start addressing the issue now so that we are no longer at that breaking point in the future.

In closing, I'd like to go on record saying I, along with my colleagues today and those that came

before me are here to support and assist you. The SEC Has a powerful voice. Let it be heard promoting diversity inclusion, and I thank you. Back to you, Gilbert.

MR. GARCIA: Mr. Hernandez, thank you very much. I'm giving you two thumbs up. Thank you, my friend. Now for our last speaker, is Mr. Michael Frerichs, who is the treasurer of the state of Illinois, and I think he really is the example of doing an exemplary job in your government service while at the same time focusing on diversity issues, that they're not mutually exclusive, and in many ways they go hand in hand, and you can do both, and you can do both great, and that's what he's doing. Mr. Treasurer?

MR. FRERICHS: Thank you.

MR. GARCIA: It's all yours.

MR. FRERICHS: Gilbert, thank you for that very kind introduction. So, good afternoon to you, Mr. Chairman, members of the asset management advisory committee, and all of our guests here today. My name is Michael Frerichs. I am the Illinois state treasurer. In Illinois, that's an elected position by the great people of the state of Illinois. It's an honor to be invited to speak with you today.

Now, the Illinois state treasurer performs man roles. Chief among them, I'm the state's chief investment and banking officer. In that role, we actively manage approximately $35 billion. This portfolio includes 16 billion in state funds, 13 billion in retirement and college savings plans, and 6 billion on behalf of local and state governments.

As an institutional investor, we have an obligation to pursue value. This pursuit encouraging corporate boards includes -- pursuit includes encouraging corporate boards to adopt external and internal strategies to promote growth.

Today, I wish to address strategies designed to increase diversity and inclusion numbers across the financial services industry in the companies in which we invest.

Specifically, I call your attention to approaches to increase diversity within the financial services industry workforce. It's utilization of diverse firms, and its service to communities dominated by people of color.

This is not new territory for this committee. The committee was formed to provide the Commission with diverse perspectives on asset management and related advice and recommendations. Nor is this new territory for the Commission. Indeed, the SEC requires public

companies to disclose meaningful financial and other information to the public. This provides a common pool of knowledge for all investors to use, to judge whether to buy, sell, or hold a particular security.

Only through the steady flow of timely, comprehensive, and accurate information can people make sound investment decisions. Commissioner Allison Herren Lee made this point in her statement on regulation SK and ESG disclosures just last month. The Commissioner pointed to the growing body of research showing the strong business case for diversity, and the importance of this issue to investors managing trillions of dollars in assets. And she pointed to research from S&P indicating that racial injustice has become a material issue with a potential to change evaluations and credit.

Clearly, this must include diversity and inclusion data throughout the financial services industry and the companies in which we invest. The public must be able to see how those in the financial industry are addressing gaps affecting people of color within their workforce, their customers, and their communities.

We know this data is available. All private employers with 100 or more employees are required to report diversity data to the Equal Employment

Opportunity Commission. We also know that too many companies in the financial services sector refuse to provide this data.

In 2018, the SEC received only 38 responses from 1,500 registrants who were asked to complete a diversity assessment report. We can only assume this refusal is embedded in either embarrassment or deceit. Embarrassment is corporate leaders know the numbers do not reflect their stated commitments to reduce barriers of entry into their workforce, promotional opportunities, and leadership positions.

Deceit is corporate leaders know the public pressure to promote unrealized diversity goals is a hollow effort without an enforcement mechanism. Today, we know it is possible to create dramatic change across the financial industry sector with relative ease, without increasing cost or sacrificing any level of service. It only takes a willingness to acknowledge past failures, and sincere desire to change.

Institutional investors, and investment consultants we utilize, also have a pivotal role in advancing diversity. We should be constantly evaluating the diversity of our management teams and staff. We should vote proxy statements, and align it with fair and equitable corporate practices. We should invest in

investment funds led by women and people of color. We should invest in diverse-led businesses addressing issues in communities of color, and we should hire financial service firms with a proven track record of equity, diversity, and inclusion.

So, I put a slide up for you to see here today. Using diverse investment firms is not only about creating growth and opportunity in our communities, but it's integral to increasing our investment returns. How do we know this? Because in Illinois, inside the Illinois Treasurer's Office, we did just that.

First, consider asset managers. We increased our assets managed by diverse owned firms from 18 million in December 2014 before I took office to $3.9 billion as of last month. That's a 216 fold increase.

Next slide, second, consider broker dealers. In 2014 before I took office, only one percent of assets were brokered by diverse owned firms. This last fiscal year, 92 percent of assets were brokered with diverse owned firms. To put it another way, our total assets brokered by diverse owned firms increased from 603 million in '14 to $43 billion in fiscal year '20.

We also engage our portfolio companies to increase corporate board diversity, which is vital to performance. We lead the mid-west in Investors

Diversity Initiative, which is a coalition of institutional investors dedicated to increasing racial, ethnic, and gender diversity on corporate boards of companies headquartered in the mid-west. The initiative has undertaken 54 company engagements, 40 of which added diverse board members, and 32 adopted a diverse search policy.

We are also a leader of the 30 percent coalition, which is a national coalition of institutional investors advocating for diversity on corporate boards. The 30 percent coalition has successfully engaged over 300 companies that have now appointed diverse board members.

Finally, we take various actions to advance equity, diversity inclusion in all the financial services industry. First, all financial investment firms that do business with our office, or seek to do business with our office, must disclose how their firms promote equity, diversity, and inclusion.

This includes a 360 degree evaluation conduct through an annual assessment that simultaneously examines and promotes diversity among board members or owners, executive leaders, owners, and suppliers.

Second, we partner with key organizations both nationally and locally, making real progress increasing

the representation of diverse individuals at all levels within the financial services industry. This includes the financial services pipeline, and the Advancing Equity in Banking Commission, both of which convene leading institutions from the public and private sector to address longstanding gaps and devise practical solutions.

Mr. Chairman and members of the Asset Management Advisory Committee, change will only come if it is required. The Commission has this authority in its rule-making power, and along with numerous other institutional investors, I have previously petitioned the Commission to exercise this power. More importantly however, the Commission itself recognizes the critical importance diversity brings to an organization. Consider the Commission's own offices, which include the office of the advocate for small business capital formation. Among this independent office's responsibilities, is recommending changes to mitigate capital formation issues, and promote the interests of small businesses and their investors.

Within the SEC itself, there is the office of minority and women inclusion that is responsible for all matters related to diversity in management, employment, and business activities at the SEC. The office of

minority and women inclusion is committed to ensuring that diversity and inclusion are leveraged throughout the agency to advance the SEC's mission to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation.

There is also the Office of Equal Employment Opportunity, which works to ensure the agency's professional staff come from diverse backgrounds. Therefore, I believe it is time for the committee to recommend four concrete steps that forcefully show the Commission's responsibility to diversity and inclusion.

Step one, Mr. Garcia, I think you'll appreciate this one. Encourage you to adopt the Garcia Rule, and require regulated entities and issuers to consider enterprises led by women and people of color when selecting firms, including broker dealers and asset managers, and to consider at least one woman and person of color when nominating directors and selecting executive officers.

This must include a consistent and required evaluation explaining why women or people of color were not chosen, and the steps needed to improve future applications.

Step two, mandate the disclosure of data by regulated entities and issuers showing diversity within

the workforce, including race, gender, ethnicity, religion, nationality, disability, veteran status, and sexual orientation. Data utilization rates for outside vendors should also be disclosed. I believe this disclosure must be made every two years.

Step three, require regulated entities and issuers to publicly disclose the race and gender of directors, nominees, and executive officers annually.

Step four, commission a study to evaluate the practices of investment consultants, including but not limited to the systemic and structural barriers for diverse investment firms.

Now, I recognize that my perspective and call to action will not be warmly greeted by everyone, and that is disappointing. At a time when the leader of the free will is ordering the dismantling of diversity training because he believes it to be un-American, we must show our country and the world that barriers to entry must be removed. Doing so is better than good business. It is the right thing to do. Mr. Chairman and members of the Committee, thank you for your invitation to address you today, and I am ready and willing to answer any questions.

MR. GARCIA: Mr. Treasurer, thank you so much. I'm speechless, other than to say I'm hugging you over the phone -- I mean, over the video camera. I'm hugging you. Let's see -- thank you so much, Mr. Treasurer. Let's see what questions we have from the AMAC committee members for our recent three speakers, as well as some of the others that might still be on, but I encourage you, you've got an incredible list of panelists, so please ask any questions.

MR. FRERICHS: I'll just say I was glad to be the diversity candidate here to show you that all Michael's last names do not begin with M.

(Laughter.)

MR. FRERICHS: I mean, half of the panelists today were Michaels.

MR. GARCIA: Yes, we appreciate that, Mr. Treasurer. Team? Well, let me say this. I'm going to ask a couple questions of my own, which is, Cheryl, is there anything that you did along the way that you said, golly, I wish I had not done that? You know, sometimes lessons learned -- some of the things that -- the bumps you learned are sometimes some of the best lessons of all. For other plans out there, for another Cheryl that's listening to you?

MS. ALSTON: Well, I'm trying to think of anything I would not have done, though -- I think we tried to be agile in terms of that, and I just really

want to applaud Illinois for a lot of their leadership in this -- in this effort. I think that one of the things that I learned along the way, and you brought up a great point about minority brokerage firms. You know, we had asked our asset management firms to use a minority brokerage firm, and within a quarter, when they came back they were in the bottom quartile, and when we talked to the firm, they said they're giving us, you know, the kind of the random trades. They're not giving us the good and the bad trades. They're just giving us the bad trades, and we don't know how they're evaluating us.

So we sat down and we -- with the -- with the asset management firm, and we said let's go through what the scorecard is. Let's talk about the evaluation criteria, and then I approved for this brokerage firm to do all of our trades, right? So, the good and the bad, let's see how they do.

Two quarters -- now two quarters later, they were in the top three out of the 20 brokerage firms in terms of performance. And so with that one of the things that I did was took that data, went to the CEO of the firm, because it was -- I've realized it was the trading booth that was kind of blocking this issue, and I went to the CEO, gave him the data, he filed it, and

he approved the firm to do trades from -- throughout -- for all clients, and as a -- as a result, they were in the top quartile for brokerage firms.

So I think one of the lessons learned is don't -- make sure that everyone knows the rules of engagement. Make sure that everything is fair, because sometimes -- and I'm not going to say they set them up to fail, but I think that just taking the first data and saying, oh, I could have just walked away and said, oh well, it didn't work, but I think really digging in and making sure that everyone understands the rules and that we are committed to this, and I applaud Illinois for their progress in terms of using minority brokerage firms, but I think as CIOs and as leaders, we're obligated to follow up and make sure that everyone is playing with the same playbook, and that they can -- everyone can compete.

MR. GARCIA: Thank you. Mr. Treasurer, first, as it relates to the Garcia Rule, that I think is the best rule ever, I think it's important to realize -- for people to realize that just because you put one forward doesn't mean they have to be chosen. The -- at the end of the day, what it means, it just gives -- everybody wins.

It gives the new firm exposure they probably

would not have had otherwise. It gives the plan sponsor exposure to a firm they probably wouldn't have had exposure to otherwise. Everybody wins, and even if the manager is not selected, or the person for a board position is not selected, just by going through the process, they'll be better prepared for the next round.

MR. FRERICHS: Got you.

MR. GARCIA: It's just about just fairness, expanding the envelope as much as possible, and you know, the consultants in my view, it's their job to source good people, to source good managers, and so at the end of the day if it's a little bit of work extra, well, that's what they're paid to do.

So Mr. Treasurer, my question to you is, you know, number one, how can we clone you to be all over America, but number two, what's happening with other treasurers? I mean, how do we get the -- I'm going to just use this term -- the Illinois Miracle out there?

MR. FRERICHS: So, a couple things, I want a brief explanation for those who are aware, this is based off of the Rooney Rule in the NFL. You had a period where more than half of the players in the NFL were African-Americans, and yet there was not a single black coach in the NFL, and part of it was just exposure and experience, and if you -- when you force them to at least hire -- or not to hire but to interview at least one person of color, what we found was their eyes were opened, and now we have done better. Still a long way to go, with the financial services industry, the same idea, although Gil, I will tell you that within the state of Illinois, my chief investment officer I believe likes to claim the Garcia Rule as named after him, Rodrigo Garcia.

MR. GARCIA: And of course, let me disclose. No relation.

MR. FRERICHS: Yes. So, to how we clone me, there's no need to clone me, but I am the product who came before me, and I am the product of people who work under me. So, two things. One, before I served as treasurer, I served on the -- in the Illinois State Senate, and every year, the Illinois State Senate would host diversity hearings for the pension and investment committee.

I was on that committee, and it was Senator Kwame Raoul, now our attorney general, who invited me to participate and talk with me about some of the faces -- some of the problems that these businesses were facing. Before him, you had leaders like James Clayborne.

So people helped educate me as I was coming along, and to the extent we've had great successes, I

think those slides we showed show that we have, this is one of the things we did first and foremost in my office was to make sure that our senior leadership reflected the diversity of Illinois.

Now, part of Illinois secret is of all 50 states, our demographic is more closely aligned with federal demographics than any other state. So that some states will have a larger Hispanic population than we do in Illinois, but our numbers mirror the federal, and some might have a larger percentage of African-Americans, but we really reflect the state.

And so diversity has been an important issue in the state of Illinois, and when I was forced to go out campaigning for this office, you campaign at all those different communities, but then when I got into office, what I found was a lot of the businesses we worked with who were receiving the benefit of our tax dollars didn't look like the people I had just campaigned in front of.

So the first step was hire people who reflect the state, because I think other speakers have pointed out, when you have different voices with different perspectives, you're less inclined to engage in groupthink, and you're less inclined to miss out on opportunities.

And then the secret is to find those people, create a vision for them -- our vision was to increase access for people of color, and two, to give them the resources they need to get this done, and because others came before me and led the way, and because there are people who are on this call who are doing most of the legwork, I get to sit here on this call and to receive your praise, but really it's a big team effort.

MR. GARCIA: Excellent. I think we have time for one more question or so. If I don't see a hand, I have one. Okay, AJ, let me ask you this. AJ, you were at New York, you left, and you came back. Was there anything you saw that changed your view of things? I mean, was there -- you know, what did you see or learn that's, like, you know, that has energized you or changed your or anything? Are there any lessons there to share?

MR. HERNANDEZ: Thank you, Gilbert. The answer is yes. I actually -- when you first started the program, you know, back in 2008, we were just learning, you know, how do we -- how do we get into this program? You know, how do we expand it from private equity to all the asset classes? I think what happened over time, you know, as we expanded, we were just thinking about the program in just one way, and having very tight

parameters around those -- you know, those programs.

When I left, what I started learning was that while it made sense when we first began the program, because we were just learning how -- you know, how to execute, how to make sure that it's done right, what I did learn was, you know, we left out flexibility, and you know, Clayton from Leading Edge alluded to it earlier. Flexibility for my manager of managers, flexibility my fund of fund managers, flexibility for staff being able to use a fund of fund manager, being able to go on a direct basis.

So when I came back that was my first priority: how do I give flexibility to allow my -- to allow my manager of managers or fund of fund managers to execute and get the best in class managers, and that's what I've been doing every since.

Same thing for staff. You know, how do we also in addition to having the extension of staff with my fund to fund managers, how do we also do that on a direct basis so that we're able to take a manager, not just put them -- put them in an emerging manager program, but also move them directly into the core portfolio?

So to me it was important, especially, you know, you know, leaving -- when you leave for five years and you come back, you come back with a different take and perspective. I think I would also add one last thing, fees. Understanding that, you know, one of the things that I've seen in the past where, you know, we've really looked at the fees that, you know, we asked the, you know, the -- or the lack of fees that, you know, we want to pay. You know, we typically -- you know, you typically see 2 and 20, and we're asking an emerging manager who needs all the capital that they can get in order to build an institutional quality back office, mid office, and front office.

I think my approach now is somewhat different. I think the approach now is I work with the manager, depending whether they are a first time manager, second time manager, a third time manager, and now I think more about, you know, instead of just getting a good deal from the very -- from the very start, which may be actually detrimental to my capital, especially the fact that I'm a fiduciary and I need my capital to be properly managed, especially, you know, with a manger with a -- with a background. And so now I look at first time managers, and I think -- I just don't think about it in terms of fees. I just think about it in terms of relationship and the big picture for the portfolio.

So I would say those are the two things that

coming back, you know, between flexibility and looking at fees very differently.

MR. GARCIA: AJ, thank you. Mr. Bernard, I'm going to just do one quick comment, and then I'll turn it over to close if I may, and that is, again, let me just say thank you to Chairman Clayton, all the commissioners, Dalia Blass, and again to you, Ed, for really making this a priority, giving me and this committee -- this subcommittee such great flexibility and runway, and I'm going to end with a quote from one of my favorite movies about diversity, and it stars Spike Lee, and of course, Ozzy Davis, a great actor, and Spike Lee is a pizza delivery man, and he's walking through the neighborhood to deliver a pizza, and Ozzy Davis who of course is the Obi-Wan of the neighborhood, and they call him Da Mayor, called him over, and he says, Mookie, and Mookie came up, and he says, always remember, do the right thing. And Mookie looked at him and said, that's it? And he says, that's it.

And I think the moral to that is sometimes we get so caught up in our daily lives that we just sometimes stray from, just do the right things, and I think we have a chance to really set things on a right path and to really address some of the barriers of entry, old injustices, old mindsets, all those things if

we just do the right thing. Thank you very much. Mr. Bernard? All yours.

MR. BERNARD: Thank you, and let me first thank all of our speakers, since that was a terrific set of panels, and Gilbert for your continued high energy and insightful leadership, so thank you very much. We are now going to change gears just a little bit to pick up on some previous work of the Committee, and we've got two different discussions, one to be led by Ryan Ludt, and one by Mike Durbin.

I'm going to -- as a heads up to the tech team, we're actually scheduled to take a break at 3:30, and I'm looking at the afternoon and thinking we put our break too late in the day. So after we get done with this next half hour, I'm going to suggest we take a quick break then, and then we'll come back for our final half-hour session, and then the lightning round. So, I'm not sure if you need to make any technical adjustments for that or not, but I'll give you the heads up.

So as I had mentioned this morning, the final two sessions are for the past work we've done, and this first one, Ryan is going to provide an overview of draft recommendations that he already sent to you regarding exchange traded products, and open it up for questions

and comments, and I would love during the course of this conversation to get a sense of whether we're generally supportive and ready to move forward, or you have questions or issues that you'd like to -- Ryan to work on a little bit further. So with that, I'll hand it to Ryan to kick off the discussion.

MR. LUDT: Great. Thank you, Ed, and thank you to all of you as well, right? This is certainly a group effort. There's been a lot of engagement from a variety of entities from you all on the committee with me, folks at your firms, and others around the industry, including some staff from the Commission, so thank you for all of that.

As Ed mentioned, this is a follow on from the work that we did in May, and the panel that we conducted around market volatility associated in March with the Covid pandemic.

We hope that we've crafted recommendations here that we can continue to talk about or revise, or perhaps move on, the idea being that these are truly recommendations on behalf of the committee. So this is not at all supposed to sound like the voice of any one, or a few -- a few folks. I definitely want to say thank you to Jeff Ptak, who is obviously very, very busy and involved in a number of initiatives for the AMAC. He participated in the panel and helped us really shape where this memo is, and also Reggie Brown, who was part of the panel from GTS, and you know, specifically helped us to kind of shape the beginning stages and ongoing efforts around this panel.

All along, this process feels like we're continuing to try to take this learning approach, where we're in this learning mode, right? We're not in fixing mode yet. In many regards, and in fact as Commissioner Roisman said this morning, this crisis is ongoing, and we feel that it's appropriate to continue to gather experts and data before launching into too many specific actions.

I think what we hope to get out of this and really convey is the SEC and the FINRA are probably the most and the best well positioned to lead these efforts, and so that's why we have recommendations involving each.

As mentioned, we've worked with each of you, and these are really our preliminary recommendations. You've seen -- you've seen a bit of a draft in mid-August. Following on from that draft we heard from a majority of you actually either saying we're in good shape, no further changes, while others offering a few topics to consider for adjustment, and we've had some

conversations ongoing following that.

Those as I get to the -- kind of the memo itself and summarize -- what I hope to do is summarize kind of the types of recommendations that we're making. They've really fallen into three main themes around trading characteristics for exchange traded products, equity market structure considerations, and fixed income market considerations.

As it relates to the trading characteristics, this really goes back to -- if you remember the conversation we had around exchange traded products and as they were trading in the market, mostly fixed income products. You had some discussion during that panel thinking about the diversions that we saw between fixed income market -- fixed income ETFs, ETPs that are market price, and their NAV, and we think that certainly warrants some more review and gathering some information there.

The next two categories are around structure and how the markets work and how I guess asset classes work. We do feel like the market worked pretty well -- it worked very well, actually, as you would hope as far as trading characteristics and dynamics work. But we also would like to see -- I think there's a way to bring some folks together and think about market-wide circuit

breakers, and what they looks like to the market.

So we've suggested a round table. I think this is where, you know, we're going to -- we're going to come up with ideas as to how we can bring experts together and study data. We don't want to be too prescriptive, so if a round table is not exactly how we pursue this and it becomes something that's more analysis and data gathering and research, that's fine. We don't want to necessarily say that this has to be a round table, but it felt like it was appropriate to ask experts to come together around the market-wide circuit breakers.

Also related to how equities work and how the market works is an exchange traded classification system. So, there's been a number of different groups working in the industry. Some industry led, some like the coalition and others.

Our peer committee really, the FIMSAC, I don't know if I can call them a peer committee, but the FIMSAC -- the fixed income market structure committee, they're also looking at a classification system, the idea being is what else can we do to help further just add clarity and add transparency as to what's going on in the exchange traded space as that grows. So those would be the two equity market structure items.

And then the last three -- so we have six in total -- the last three items are around fixed income market structure, two, regarding trades, that has to do with trading transparency and how and when trades are reported, and what information and how that's available for bids and offers in the fixed income space, and then lastly looking at more broadly the characteristics of the fixed income market, and are there areas that we can continue to evolve there that would help with transparency, price discovery, and liquidity? So, those are our six recommendations following on from the work really bucketed into those three areas around trading characteristics and market structure.

So hopefully each of you have had a chance again to look at where we are with the memo that's been shared for a few days. We really value your input and your feedback. We're happy with where we've gotten to now, but we'd love to hear what questions or thoughts you have.

MR. BERNARD: Any questions, comments, concerns, suggestions?

MR. LUDT: And I'll try to thumb through the grid as well. I -- let me know if you see anybody, or please speak up. So, I see Rama with a question?

MR. SUBRAMANIAM: Yes. A couple of related questions. I notice on the -- you know, the recommendations on the equity market structure, you referred to a fixed income market structure ladder, and then similarly, you know, the last lot of recommendations around fixed income market structure, I would have thought overlaps maybe with some of the work on the fixed income market structure committee. What's the -- maybe it's a process question, or maybe not that important, but you know, it seems to me that this kind of falls between maybe the two committees, and what's been the dialogue with them if anything, or have they considered similar things? I'm just trying to work out the overlap.

MR. LUDT: Yeah. I'll take a shot at the beginning of that. We have not had -- we have not had conversations specifically with FIMSAC. We're certainly aware of the work that they're doing, and how they're thinking about approaching those aspects in the market. From a process question as to whether it relates to our committee or theirs, it certainly is independent of those two.

We viewed it -- I viewed it as we would want to make the recommendations independent of or regardless of what another committee is thinking about, and hopefully each of us is kind of working in parallel or

in tandem to bring ideas and thoughts to the SEC.

MR. BERNARD: Any other questions or comments? Can I -- I get a sense -- so that this is our first stab at approving actual recommendations. I think we all agree that it's -- you need a team to go away and draft something -- a document such as this, and I think they've done a superb job as opposed to having it drafted by 22 people, but we do want to have the input -- and Ryan, as I said -- as he said, has gotten a fair bit of input from folks and support from the committee.

Does anyone have any concerns with the document as written? Let me -- so, apparently know. Can I just sort of see nodding heads? Are people generally in agreement and supportive of what they see here? Now I do see lots of nodding heads. In that case, I'm not sure I need to belabor it. Maybe I'll just ask. I think I'll ask us to formally approve this to go forward as recommendations.

In my view what I think is great about this is that first of all, I think the panel in May was superb in terms of helping us hone in on the key friction points that were experienced and sort of the issues that were highlighted by the activity. This was the ultimate tabletop exercise that no one would ever

actually undertake to have the markets go through what they went through, and to see what kind of stresses were revealed.

I think the recommendations also speak to the unique position of the SEC to bring together the different players and parties in the ecosystem to, as Ryan says, continue to advance the learning. So, I'm going to ask three questions. Since -- because of the format we're in, we're not all in the same room. I'm going to ask if you're in support of moving the memo ahead, if you approve it. I'm going to ask for any that don't approve, and/or any who abstain.

So, I'll go through all three of those to see where we are so that no one is left out, and the only way I know to do it is to ask everybody when I do that is to ask you to unmute so we can hear your answer, and if there's echoes it's okay. We just need to hear yesses and nos. So with that, if everyone who is supportive of moving this forward as a formal set of recommendations, please say aye.

(Series of ayes.)

MR. BERNARD: Okay, and with anyone who is not supportive or still has concerns, please say nay. And anyone who would like -- choose to abstain from the vote, please acknowledge. I think you got it done,

Ryan.

MR. LUDT: We got it done. We did.

MR. BERNARD: So I thank you -- thank you all very much for that. I'll take an audible on the field here. I promised to take a break at this point. Should we go ahead and do that, and then have time for Mike to do his piece? I'm seeing some thumbs up for break. It's 2:45. It's come back at 2:55, at five minutes to 3:00.

We'll take a 10-minute break, get away from our screens, and then we'll come back and have a similar session with Mike Durbin, and then do our lightning round, and if we get done a little bit early today, that would be terrific. So, we'll be back in 10 minutes. Those on the -- who are watching on the webcast, you'll see the holding screen -- the holding slide for about 10 minutes. Thank you.

(Whereupon, at 2:45 p.m., a short break was taken.)

MR. BERNARD: All right, thank you all. I'll sort of be mindful of the breaks in the future and get those in the right place.

So we've got one final session discussion led by Mike Durbin and then we'll do our lightening round, and if we get out a little early that will be terrific

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I'm sure.

So for this final discussion you will recall in May another of the panels around operational issues that Mike led, and like Ryan with ETP he graciously agreed to sort of continue the work there, because again we think there was so much evidence provided by the response to the pandemic. And in this case it wasn't just the volatility in the markets, but it was also operational issues such as essentially everyone being forced to work remotely and the impact that had on a whole range of issues.

Mike is in a slightly different place and asked to take advantage of having the group together to seek some input. So I think what Mike is going to serve up here, I'll let him tee that up, but it's more a sense of here are the priorities that he and the drafting team are focused on and he wants to get input from the group on are these the rights priorities and any color commentary on that, and then he'll come back to us with a draft.

And let me just with that actually, rather than steal your thunder, Mike, let me turn it over to you.

MR. DURBIN: Thank you, Ed. Everyone can see this okay and here me okay? So thank you, Ed, and to my

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fellow AMAC members as well as the Commission on, you know, being given the chance as Ed said to update everyone on the work that we've undertaken regarding the series of operational challenges that manifested themselves pretty acutely in those early stages of the pandemic.

I want to particularly thank Neesha Hathi, my partner in a lot of this work, but also believe it or not members of many of your firms that this work has been able to reach into over the last several months. So I represent a fairly complex effort around this. It's by no means mine alone, but you're going to have to listen to my voice for the next few minutes if that's okay.

So again as mentioned here already this morning and just now, you know, we're not here to approve a final set of recommendations, but I'll endeavor rather to update you on our work and then how our refined set of priorities ha emerged since we first talked about these at the end of May, which based on the feedback either today or what follows today will form the basis of the more formal step of recommendations that we'll ask the AMAC to consider in the coming weeks.

The overarching theme to what I'm going to share is really to make permanent a number of temporary

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relief items that the SEC and others did give to the industry, honestly on a very timely, practice, productive and healthy basis in those earliest day of the pandemic.

So we're going to offer, you know, the draft recommendations that are going to follow here after this slide in order to improve, you know, as Ed alluded to, select core processes that were impacted due to specifically the health and safety concerns brought about by COVID 19.

These recommendations seek to minimize the need for physical processes in favor of leveraging more efficient, and safe, and increasingly adopted digital alternatives. As mentioned, the recommendations to be discussed are designed to be permanent regulatory changes that provide viable long term solutions for investors and the industry and not just short term relief for the duration of the pandemic.

We do think it's important to really specifically flag here that care has been taken to only flag those areas for consideration which have clear attribution back to the pandemic related issues or concerns. That's a fancy way of saying that we didn't take advantage of the invitation by the Commission to make a series of recommendations and throw things into

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the consideration set that are not explicitly tied back to the issues that were incurred by virtue of the pandemic. So we tried to be disciplined there.

The recommendations that we're likely to put forward, but ask your continuing consideration and comment about, fall into these five broad categories, which if you'll indulge me just because I'm unmuted and have the screen I'm going to run through in their entirety and then we'll open it up for discussion.

Working left to right, the first starts with E delivery. It again bears mentioning that our AMAC voice here is but one of many that the SEC is hearing, has been hearing around this broad topic of E delivery. So it's in that context, you know, we likely will submit the SEC could update its rules and interpretations incorporating appropriate investor protection principles, which I'll come back to, to permit firms to use an investor's digital address, such as an email or Smartphone phone number as the primary or default address when delivering regulatory documents, and should work closely with FINRA and the MSRB to evaluate and importantly harmonize their SRO rules with any SEC digital delivery amendments that they choose to take on.

Similarly, the SEC could amend its rules that currently include requirements to provide investors certain documents in writing instead of the requirements to furnish or provide such documents, which would recognize transmittal through these more digital means.

And again as I referenced, any recommended policy changes should incorporate essential investor protection principles that include, you know, things like clear notice, alerting investors of a switch to electronic default delivery, that permit an investor to affirmatively choose paper and change that preference at any time at their discretion, and that provides safeguards to address invalid or inoperable digital contact information.

So that's E delivery in a nutshell, and again I'm going to keep plowing ahead and we'll cycle back here to any of these if you'd like when we open it up to discussion and Q&A.

Second column here is really around recommendations related to this remote work paradigm. So, you know, the pandemic did trigger an unprecedent shift in the workforce for all Exhibit A here, you know, the work from home paradigm for many financial services employees, including importantly registered employees in this context.

So the shift has created a series of challenges, including the inability to comply with

existing obligations, by example FINRA Rule 3110(c), to perform onsite inspections of a branch office.

So acknowledging the unacceptable health risks of onsite inspections due to the pandemic, FINRA provided welcome temporary relief extending the period in which broker/dealer firms can permit their 2020 annual branch onsite inspections to March 31st of 2021.

However, due to the continuing nature of this pandemic and likely future travel restrictions and health and safety concerns, this extension is unlikely to be sufficient. So again it's in that context that we're considering the recommendation to adopt more permanent relief.

So specifically the SEC could direct FINRA to modernize the internal inspection requirements of FINRA Rule 3110(c) to permit remote technology assistance inspections by firms. The SEC could direct FINRA to revise its branch office registration and inspection requirements, including the very definitions of branch office, office of supervisory jurisdiction, and the inspection requirements that are attached to those designations in light of advances in technology and telecommunications.

The SEC also could direct the North American Securities Administrators Association or NASAA and FINRA

to make permanent remote testing capabilities for the Series 63, 65 and 66 securities licenses, and expand online testing capabilities to cover all qualification exams.

And the finally the SEC could further extend the relief for mutual funds from the requirement to vote on certain matters at in person board meetings. We may also recommend, it should be an interesting one, that Congress, because it would take an act of Congress, consider amending the Investment Company Act of 1940 to remove the express statutory requirement for in person board meetings. These are the elements of this environment that are just quite tough.

So that is the second broad category around the remote work paradigm. If I move on to the middle column here, recommendations related to more of an E authorization sort of standing. The pandemic has increased the difficulties, there's a theme here, associated with obtaining customary types of authorizations that are required by the SEC, FINRA and state rules and regulations. These include the manual signature requirements pursuant to, by example, SEC rules and regulations like a Broker/Dealer Focus Report, Form 144, et cetera, notarization requirements including for IRA purposes and the medallion program that's used

as a valid signature on many documents, including those related to corporate actions and negotiable documents such as physical certificates and related paperwork. So again the SEC has provided flexibility regarding manual wet signatures in the current extraordinary environment, however the safety and security of industry employees and investors requires minimizing the need for physical processes or physical artifacts in an era of rapidly improving and utilized digital alternatives.

So the SEC could permanently adopt rules that allow for more, these more digitized methods of authorization, including those related to manual wet signature requirements, notarizations and medallion stamps, and they can importantly in coordination with FINRA, other regulators, including at the state level where applicable because same of these are applicable at the state level. That is E authorization.

On the fourth column here, recommendations around dematerialization, this experience group knows that although most U.S. securities are offered in paperless form certain asset classes continue to issue physical certificates of ownership. And so while the number of physical certificates process has declined over the years, the fixed infrastructure to process

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physical certificates remains. Therefore, the cost to process the physical certificates that do remain has increased, with many of those costs being passed along to investors.

Moreover, and that's why we're talking about it from a risk management standpoint, an industry decision to immobilize physical certificates in a central location has been problematic during events such as 9/11, super storm Sandy, and our own COVID 19 when market participants have experienced issues regarding the ability to gain timely access to the inventory of those physical certificates.

So it's not lost on us that this theme, this dematerialization, you know, is a theme that would require intense coordination across multiple industry stakeholders. So our recommendation is really -- is likely to submitted in that context, you know, to be reflective of the complexity. So as we state here on the slide the SEC really could hold, starting with a staff roundtable on the topic of further dematerialization of physical paper, inviting the views of all these various stakeholders, which include, you know, issuers, transfer agents, broker/dealers, clearing corporations, banks, investors, regulators, various industry experts to help inform future continued SEC

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action on this topic.

And then the fifth and final, rounding it out here, and I'm going to pick up a little bit from the Garcia Rule of lessons learned, which he asked, you know the panelists, in our view great organizations are learning organizations and great learning can come from detailed after action reviews.

The reality is a lot went very right, you know, by the SEC and others in the darkest moments of the crisis but, you know, but like many other industry participants already are doing, you know, could the SEC similarly conduct and document a more fulsome after action review of the steps taken, the sequence pursued, the parties needed to convene, et cetera, in a way that would provide incremental efficiency and in the, I hate to say it, in the event we find ourselves in a future crisis situation, would perhaps provide a bit of a head start.

So this is no way meant to hold ourselves or the Commission out to s standard to have a detailed playbook for each and every unimaginable future crisis, but rather again accounting -- an accounting of the broad steps taken or that could have been taken to ensure, you know, maximum sort of efficiency around communication, mobilization, transparency, relief, et

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cetera.

So those are the five broad categories. Hopefully, a bit of texture or detail around, you know, some of the underlying attributes around each of these broad five categories that we would like to pursue in the context of a future, more formal recommendation. We do tee up here just in the spirit of trying to get a conversation going or in the interest of answering any questions anyone has.

If you think about those five categories some of the more detailed ideas that I've laid out here, that we've laid out, are just the mouthpiece. Are there additional areas that we should have considered, have we missed anything, you know, blatant? Do the above considerations strike the right balance? Because we fell pretty passionately that there should be an appropriate balance here. And how would, or should, or could the AMAC prioritize, you know, these areas in our recommendation to the SEC, to the extent that we feel that a further prioritization would be necessary or prudent.

So, Ed, I'll pause there and in that spirit invite any questions or debate.

MR. BERNARD: Okay, great. If that's you sharing -- yeah, there you go. I think if you give us

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the screen back.

First of all, I'm glad I was -- stopped talking and stopped stealing your thunder because your remarks were considerably more cogent than mine. So I thought that one slide captured a lot, and appreciate the work that's been thus far.

Now is a great opportunity for the Committee, since this is still work in progress, any questions, comments, anything, including if you think it's on the right track. I mean, it's not just if there's confusion or something, just to help Mike move this forward.

Again, given the immediacy of the events, how quickly the SEC responded to it in the midst of -- in real time, and as Mike mentioned the fact that other voices are beginning to weigh in, and I think I mentioned this this morning, I'll work through the procedural details with Christian, and Dalia, and others, but my expectation and hope based on the input from this group is that Mike and team will bring this together fairly quickly and we will call a very brief meeting, not a full day meeting, sometime later this fall rather than wait for our December meeting to act on formal recommendations.

So this would be a great time to weigh in with any questions, comments, or concerns.

Thanks. Scot.

MR. DRAEGER: Yeah, thank you, Ed, and thank you, Michael, and everyone who worked on this spectacular work product. This is exactly what we needed and right when needed it. So I just affirm everything that you've put forward.

My question for you is just about segregating the things where maybe time is of the essence versus the things that may require, you know, suggested roundtables or deeper deliberations and studies. I know that a lot of us, and Mike you and I talked about this, I know personally we're very -- you know, and it weighed heavy on our hearts that some of the folks in the mailrooms, and printshops, and paraprofessionals trying to track down the wet signatures for trust agreements and things were the people being required or asked to take the greatest risks during the heightened elements in the pandemic. Knowing that we may very well be back in a situation closer to what we experienced in the spring as we head into the winter, do you envision segregating the efforts on things like E delivery to prioritize, you know, those type of things, wet signatures, things like that out to try to get the Commission to move on some of those things, maybe even a little further along than they

have, and then have things like dematerialization studied a little further? So I'll stop there and also just say thank you.

MR. DURBIN: Well, thank you, Scot for your comments and the question. Yes, you're term, you know, sort of segregation or segmentation is really another, another riff on prioritization.

And so if you believe in subliminal advertising, to my fellow AMAC members, those buckets of five categories left to right, there's an implicit prioritization that we think could be actionable there. And it is -- they've been drafted exactly, Scot, along that dimension, things that are quite timely and would have, you know, the desired impact for sure, and a little dose of inexecutable, you know, so there's both sort of a supply side and the demand side element, you know, to the prioritization. It's implicit in how those five categories have been laid out there.

The dematerialization or future crisis playbook, you know, they have less of that urgency and are complicated, you know, to do, particularly in the case of dematerialization just given the range of stakeholders that would have to be involved.

MR. BERNARD: Other questions, comments?

Michele.

MS. BECK: Just a brief comments. I really do appreciate the points about branch inspections. It is the time of year where we try to figure out will we have to employ a surge labor force to go out to people's home in the first quarter of the year before that timeline runs out. So that's -- the planning is now and so we really appreciate the issue being raised now.

MR. BERNARD: Ryan.

MR. LUDT: Hey, yeah, I'll just add another brief comment, and Mike sorry I haven't gotten comments on each of these back to you yet. Our initial look certainly prioritizes that E delivery topic as probably numbers one, two and three. That certainly feels like the highest priority for us, and I can just simply say we're working with others in the firm now. I'll get you comments back as soon as possible on the other items.

MR. DURBIN: That's great. Thanks, Brian.

MR. BERNARD: Anybody else?

Great, and can I just sort of, like, from like a nod of heads, do I have agreement that if we can turn this document around and get a meeting on the calendar that we -- you would be comfortable moving this forward promptly. Okay, I'm seeing lots of thumbs up and nodding heads.

I do want to also just close this -- I won't stretch it out if people seem to be comfortable with the direction, to pick up on something Mike said, that a lot of this is about making permanent some temporary rules that the SEC put in place to allow for orderly function during the crisis.

Two things. One, in fairness to the SEC, doing a permanent rule requires probably a heavier lift than a temporary, so we understand that there will be some work to be done on these recommendations. But really to come back to we all know from direct experience what it's like to drink from that firehose when it's happening in real time, and I have to say from everything I can see the SEC and their partners at FINRA were extremely responsive in the moment to help the industry do what we were supposed to do, which is to serve and protect our investors. So kudos to all of them for that and for their colleagues at the Fed for helping keeping the financial markets open and so forth. But I think interestingly this list is something of a tribute to how much they got done in a very short period to enable us to operate.

So if there's nothing else on that, as promised we were -- we're ahead of time, which is a wonderful place to be, we'll finish out with the lightening round. And to refresh you on our standard approach to lightening round, I'd like to -- and I'll just, actually I'll gives a heads up. I'm going to go -- I went reverse order time, I'm going to go -- if you're looking at the participant list I'm going to go alphabetically by the screen name, which in most cases is first name.

So Alex Glass, you're going to be up first. But it's real simple. Just take no more than a minute to share one or two things you heard that struck you today. In addition to what we discussed for today I'd be particularly interested at the three issues that you would prioritize for further work by AMAC.

And to be clear, if what struck you is the same as the six people before you, that's fine. This is not a creative writing exercise. You can feel free to say the same thing. That will actually give us a sense of, boy, that was a really dominant theme. So don't worry abut redundancy, just speak what's on your mind. But of course feel free to raise new issues if you'd like.

So with that, and I'm going to go through the list and then I'll see if I missed anybody. It's kind of hard to work from this participant list, but I think I've got it. So Alex, you're up first if you would.

MR. GLASS: All right, very good. Can you hear me?

MR. BERNARD: Yes.

MR. GLASS: All right, great. So again I thought the discussions were spectacular again today. I always take a lot from these meetings. As a regulator I'm always looking at the topics in the lens of investor protection, which is also -- while also being cognizant of a lot of the impact on the industry that I think was talked about today.

So then a few things that really struck me today, and going all the way back to the beginning of the meeting talking about ESG, is degree is a very important topic to determine what's meaningful for investor disclosure. I second Joe's comments about the advertising and marketing is something that really needs to be considered because investors really don't dig into those prospectuses, so it's something that really needs to be out front for those investors.

And then on Mike's operations discussion, very supportive of -- I'm very supportive of innovation in Indiana, and you can see that from a lot of the actions and things that we've done over the past several years that help both the industry and regulators while maintaining that proper investor protection. So I like

that Mike was adamant that all changes must have that investor protection component and safeguards, and I really look forward to those continuing discussions to look for ways to be innovative and make some of these temporary solutions permanent.

MR. BERNARD: Great, thank you. Aye Soe.

MS. SOE: Thanks. I thought -- well, I was very interested in the discussion on the ESG as well as private assets.

With regards to ESG I agree that the advertising of ESG funds, and in particular what is concerning is in light of COVID 19 crisis and the performance, the fact that they beat the benchmark is being used to attract, you know, assets and used to promote, to highlight the effectiveness of ESG when if you dig into the research it indicates something else. I think that part needs to be understood, so the advertising probably needs to be looked at.

In terms of private assets I'm a bit torn because I do believe it's one area where more and more capital is flowing and it's important for regional investors to have access to returns. At the same time, you know, I was very interested in the presentation by the academics on some of the pitfalls and also the use -- the metrics to measure and how do you compare private

returns to public market returns.

So there's a whole chemistry, but that's my personal takeaway from that.

MR. BERNARD: Great, thank you. Erik Sirri.

MR. SIRRI: Yeah. I just -- relative to Mike Durbin's presentation, I thought the wet signature was definitely an issue. I know from talking to our complex it's kind of a high priority. I don't know anything about how complex it is, but I know it was quite a sticking point in just getting work processes done, so I think they will be glad to see that there.

On privates I just observed that, you know, while there's some real issues with disclosure and reporting potentially on the performance and risk side, there does seem to be a colorable case for including privates in a retail portfolio. I think before long that group is going to have think about the details of what form such an investment would take, what are some of the -- you know, what kind of pooled vehicle it would be. So in that sense we've got our work cut out for us, but I think it's probably worth starting on that process.

MR. BERNARD: I'm just going to leave myself unmuted. Gilbert Garcia.

MR. GARCIA: Sure. Thank you. I guess for me the privates also was very interesting, but I guess I'm of the view I think getting retail involved is going to be a lot harder than we realize for them to have the actual, all the sophistication or all the disclosure, and I just want us to be careful that we're not sowing the seeds for the next bailout or something of that nature.

MR. BERNARD: Nobody likes the word bailout so --

MR. GARCIA: No, noted.

MR. BERNARD: Jane Carten.

(No response.)

MR. BERNARD: I think we've lost your sound again, Jane. Are you muted?
I see her saying no. Given what we went through before, Jane, I'm just going to keep going if that's okay. Can you give me a thumbs up? Sorry about that.

Jeff Ptak.

MR. PTAK: Yeah, thanks. I think the previous respondents have covered it pretty well, so I won't belabor any of the things that they already covered other than to say I found the, you know, the private markets discussion reinforcing in some ways. I think, you know, it's a laudable goal to expand access to

private markets so that, you know, so-called retail investors can also partake in it but, you know, it's also fraught with some complexity and difficulties, you know, as we saw several of the panelists kind of delve into that, whether it's advertising or the very definition of the performance stream that an investor has been able to realize over the course of their investment.

There's just a number of pitfalls. They're not sort of the sort of thing that I would say preclude consideration of it, but it does highlight I think some of the tradeoffs that, you know, the industry will have to, you know, basically confront as they're bringing this to the broader investing public.

As I may have noted at our original AMAC meeting, it does give me some pause just knowing what we've observed investors using, you know, mutual funds, liquidity products. I feel like a progress has been made there, you know, in part attributable to innovations like the target day fund, which I think ultimately served to simplify the investing experience and remove some of the complexity and decision making that would otherwise attend to it.

And this kind of goes to the other direction, though it does boast a number of other salutary

attributes. So -- so it just -- it helped me to appreciate some of those tradeoffs in an even fuller way. So that was my main takeaway. Thanks.

MR. BERNARD: Great, thanks. Adeel, you're next. Your last name is on the list.

MR. JIVRAJ: Sure. So first of all I thought today's agenda was great and certainly covered a broad range of topics. It reaffirmed the complex issues that we're exploring, whether it's ESG, private investments, or diversity and inclusion.

On the ESG topic I was just wondering if third party verifiers could play a role in the trust and verify aspect of it if a framework is ultimately developed. It might help from the advertising or the disclosure aspect of it.

I'm also looking forward to regrouping with the private investment subcommittee and to debrief on what we learned today from our panelists. Certainly, a lot of was shared on the advertising front from Ludo as well as some of the benefits of including the fact the last two weeks of investors. So I do think and I agree with Josh Lerner that there might be a place for these types of investments in an appropriate structure, but certainly willing to learn more as we debrief and we further explore it in the subcommittee.

And then lastly I just want to commend the Committee in creating a subcommittee on diversity and inclusion and certainly looking forward to continuing work in that area of the Committee as a whole.

MR. BERNARD: Great, thanks. Joe Savage.

MR. SAVAGE: Thanks, Ed. So I thought all the panels were great. On the ESG panel, I thought they did a really, really good job of kind of showing the complexity of the issues that are in there.

But, you know, my view, and I think it probably reflects their views as well is that, you know, you don't want to let the perfect be the enemy of the good, and I think one of the, one of the panelists said that. So it's going to be kind of an incremental approach my guess and it's, you know, you'll have to try some things that may work, it may not work, but I do think it's worthwhile moving forward and finding ways to standardize or at least better disclose ESG funds so people kind of get the message better.

And then like Adeel I'm on the subcommittee for private investments and I really liked that panel as well. I think we really need to -- you know, if we're going to expand access to retail improving advertising standards, performance standards, disclosure standards, and any curation that needs to occur needs to go hand-in-hand with that. It can't just be an open door. So just speaking for myself. Thanks.

MR. BERNARD: All right, thank you. John Bajkowski.

MR. BAJKOWSKI: Yeah, again, a number of really wonderful and interesting panelists today. In regard to the ESG thing I have to really just -- again the notion of disclosure, the use of the AMAC, it was revealing to understand the impact of even the use of ESG, whether it is an asset class and whether funds are held accountable for what they do with it, truth and labeling issues. I think the disclosure with some sort of standardizations of disclosure is very helpful in that regard.

And with the private investment, I mean you can't ignore that. There's a tremendous growth in assets under management through private investment. The challenge is how do we open up that market to the retail investor in a way that they understand the risks. You know, there's not even a clear understanding of whether or not there's an outperformance of them, whether or not there's an addition to return or diversifications seems to be a benefit that.

So I think there's a lot of work to be done as far as the element of disclosure and protection of any

investors that want to participate in private investments, private equity, and understand that there's a time element to it. So I think there's -- it's interesting information, but the question is how, how can we safely open up those markets to the retail investor and understand that their knowledge is an ability to understand those risks and is quite various over, over different groups.

MR. BERNARD: Great, thank you. John Suydam.

MR. SUYDAM: Yeah, very good panels, interesting discussion in lots of different areas. The thing I was most struck by was on the ESG third party validation. What struck me most about it is it doesn't seem like there at this point is enough coalescence around what's being looked at, how it's being measured, you know, which maybe a limiter on any standardization in the area, and I think we probably need to get some better understanding of that as we move along with any potential recommendation.

MR. BERNARD: Great, thanks. Mike Durbin.

MR. DURBIN: Yeah, just one, one quick observation on three broad topics. First on the ESG, echo the views of other AMAC members. Really hats off to the team for wading into the deep end of complexity there. It was impressive.

I'm particularly struck by this healthy tension I guess between the ratings or disclosure issue at the fund level versus the underlying issuer level. We just submit that we as a non to the issuer level remember that some of this ESG enthusiasm will be rendered outside the context of a fund or an investment adviser relationship. It will find its way in brokerage too. I want a basket of green stocks.

And so getting to the issuer level I think has a role there, certainly on, you know, sort of disclosure if not, you know, an underlying rating system.

Privates, Erik Sirri, thank you for asking. You asked before I did about liquidity because that -- we talked a lot about a lot of different things except liquidity and I think that is a principal fulcrum around just how inclusive do we make privates. Because people can tolerate liquidity, illiquidity until the day they want their liquidity.

And then on D&I, Gilbert, you know, kudos to your panelists because to hear directly from consultants and major public pension investors of just how in motion they are on this issue is, you know, another very healthy wakeup call that we're well on our way. So I thought those were excellent perspectives, you know, from real life, real business going on, so thank you for

those.

MR. BERNARD: Michelle.

MS. BECK: Great, thank you. The private assets panel was fantastic, really enjoyed all the points made there.

And it occurred to me when we're looking at this question of do the returns align between private and public markets. Liquidity was one piece that should cause a different. You should get a premium for private assets because of the illiquidity in them. But there was another element that I was struggling with, which is the appraisal based nature of the NAV calculations in private equity and private assets versus the constant price discovery going on in the public assets.

So I think there's a second premium that you should expect with private assets. And so it's nice that there are times when they do outperform, but boy they better because those two premiums need to be baked into hat return stream.

So it also made think about, you know, the question about what kind of liquidity should the retail investor have. So with mutual funds daily liquidity is in place, even for retirement funds. Now you move your retirement funds sometimes when you reallocate, but the idea that you need constant liquidity even in those kinds of funds is sort of expected, and yet it is a question mark for me. You know, there -- people can earn a premium by taking less liquid assets on those monies they should need the cash out too quickly. And it's just worth thinking about, is it the case for the retail investor that we always expect them to be able to cash out very quickly, in which case private assets are not a good choice for them. But if we're able to tolerate a little bit more illiquidity for the retail investor then there might be a spectrum which should placed in, you know, illiquid assets and the like.

So when it came to the diversity and inclusion panel I am still thinking about how do you -- how do you consistently address the larger institutions that are -- and make sure that -- one metric that's terribly important, you know, women, minority owned businesses, over 51 percent or I've heard 25 to 49 percent, but what do you do for the big companies, what are you looking for. And what occurred to me as I heard folks speaking is it is terribly important to focus on the senior ranks rather than broader measures of inclusion because the -- there's still quite a group as folks were telling us, there's still quite a difference in the senior ranks in

a lot of companies than there are across the company overall.

So I thought that it would be good to folks on more than one metric and it would be good to hear the panelists talking about more than one metric would be a useful tool to ensure diversity of decision making.

I was also reminded that there's a great book called "The Hour Between Dog and Wolf" that talks about gender diversity and actually age diversity in the workforce based on some of the different biology of people of different ages, and very structured studies of risk taking behavior that differs between genders and between ages. It's worth a read again for people that may be skeptical about diversity and decision making is really as much of a value as we're placing it to be. I think there's some really good empirical proof that it's a good thing to be looking at. The book is a very entertaining read.

MR. BERNARD: Thanks for that. We'll have to add reading recommendations to future lightening rounds. That's great. Neesha. I think you're muted.

MS. HATHI: Hi, sorry about that. I was just writing down Michelle's recommendation. I thought I had read every D&I book out there, so thanks for that. I'll echo the sentiments of everyone else, just really

complex, great topics today.

Starting with the ESG, I think, actually I think it was Michelle you said this around, as the next step, getting more investor feedback with regards to where we go. Because I think one of the things that really struck me is, you know, talking about disclosure versus things like naming and rating. I think about, you know, the mainstream that we serve disclosures, you know, are one thing, but it's really different when it's very obvious in naming and rating. There are things that we'll use a shorthand to make sense.

So that sounds likes a really great next step and clearly a very complex topic.

I really enjoyed the private investment panel and I think from the standpoint of, you know, if we believe that retail investors should have choice and should have access to where wealth is being created, I think, I think I would suggest that this is an area that we should continue to pursue. I wonder when we do that, and I actually -- some of the comments just made me think about, you know, what are the steps that could be taken sooner rather than later to begin to create the type of environment that would allow a retail investor to have the information they need to make educated decisions, so, you know, the transparency needed around

pricing, the transparency needed around valuation, you know, potentially the metrics around IRR and other kind of advertising uses to talk about the performance of the investment.

So I just thought that there was a lot to do there before maybe we could take the step of really making them broadly available.

And then on the D&I side, the comment that really sat with me was the embarrassment versus deceit that I think our panelists, the Illinois treasurer mentioned. And I, you know, I just -- I think it's kind of something that we continue to talk as a data driven industry that we're not really getting the data in an area that, you know, would really probably be helpful, and then once you have the data you can decide how to operate. But right now the data is still in terms of, you know, the actual D&I practices within the industry are still just a little --

And I think you all know where I stand on the operation topic that Mike already walked us through, so I won't say anything more about that. Thank you.

MR. BERNARD: Great, thanks. Paul Greff.

MR. GREFF: Thanks, Ed. So, yeah, just a couple comments. I'm thrilled to be invited to be a member of the diversity and inclusion subcommittee.

Thank you, Gilbert. It's an area of great interest to me to be a worthy contributor.

My second comment echoes a comment made by Commissioner Crenshaw in her opening remarks. I will be interested to see how, if at all, the ESG Subcommittee considers the output of other federal regulators, such as the Department of Labor, the CFTC's Climate Related Market Risk Subcommittee when developing its final recommendation, because both have put out statements recently that are quite divergent. So I will be interested in that.

But kudos that team for putting fort another ridiculously through presentation. So thanks, Ed.

MR. BERNARD: Thanks. Rama.

MR. SUBRAMANIAM: Thanks, Ed. The ESG panel was very interesting for me. I think a couple of, a couple of things for me like the name standard what's left out I found surprising. There's a lot of complexity there and they're trying to wade through that complexity and get some, some standardized disclosure I think is important. But there seems to be, like, a lot of things that I know Michelle is working through and almost kind of narrowing the focus I guess is one of the hardest things. It's such a wide area.

On the private investments subcommittee, the

panel was even better than I had expected and kudos to Erik for moderating that and, you know, I wish we had more time for questions.

I would encourage people to respond to a short questionnaire that we will be sending out, Joe Savage will be sending out, to elicit feedback on the design principles. I think everyone, most people at least are, you know, getting to that key topic of balancing investor protection with investor choice and, you know, how do you balance that, how do you find, you know, the right middle ground that if we find a way forward. So it's really good to hear from people.

You know, as Ludo himself said there is a very well developed disclosure regime in the mutual fund world, which is the registered investment company, right. So we should, we should not be put off by, you know, some of the comments about the advertising and IRR because all those are disclosure points, which are solvable within the right framework. And so I encourage people to provide their feedback on the design principles that will help us take that topic forward.

MR. BERNARD: Great. Rich Hall. Technology is working.

MR. HALL: I guess there were two areas that I wanted to react to, one was the diversity and inclusion

panel. That's a topic that's important to UTAMCO, and actually we were acting on it before it really came to the forefront of all of our minds in the spring and summer. It was on our management team's annual priorities a year ago.

So thanks to Gil for bringing, you know, resources and thinkers on this topic to our attention and everybody's attention. It's super helpful.

You know, we responded, we -- I don't know how many of you are aware but Congressman Kennedy and Cleaver sent an email to a lot of the top endowment asset managers and asked what our exposure was to diverse, diverse managers. So we responded to that. You know, I would say we benchmarked well relative to the industry's current -- you know, the status that basically is called out in the Knight Foundation. But we recognize that there's more to go and we're focused internally and externally on how we expand our firm diversity and then the diversity of the managers that we employ.

I do agree with Michelle that I think we should consider how to be a little bit more expansive and inclusive in what we're looking at, right, when you get to the large firms that we kind of default and have to work with some large firms because we have a lot of

money that we're trying to manage and we have a very small staff to do it. So we can't have a lot of small investments just -- it's to a degree inefficient.

So how do we, how do we look at the large firms and how do we look at expanding that threshold. Maybe we should have used the same parameters when we responded to the Kennedy and Cleaver letter and applied 25 to 49 percent, and I think our numbers would have increased even further. But we should be mindful of that. Let's not put too much form over substance. Let's make sure we're really getting into the inclusiveness of it.

And the second thing that struck me was the private conversation, private assets, a scenario where I've spent a lot of time in my career. I think we should first try to decide how or if the investor universe will be expanded and do that before you decide on what regulatory changes you want to make.

The sophisticated investors, you know, if you're in the institutional or accredited investor category, you should have the resources to be able to understand what is being put in front of you, and if you don't understand you shouldn't do it. That's the bottom line in terms of untangling the various performance claims that are made and understanding what you're likely to get at the end of the day.

The reason I say that we should figure out first whether we're going to expand the investor universe before you do more regulation is that regulation comes with a cost and ultimately UTAMCO and the pension funds, we're the ones who bear the cost and it gets passed back through, to us to a large degree it gets passed back through to us in the management fee and all of the charges that flow through a partnership agreement.

And so you're taking money by forcing more regulation. You know, you're taking money out of the pockets of the pensioners or, you know, the students who benefit from the scholarships that we're trying to invest, and preserve, and grow. So I would just say let's be thoughtful about that before we add cost into the system. That's all I've got.

MR. BERNARD: Okay, great. Those are helpful thought, thanks. Ross Stevens.

MR. STEVENS: Sure, Ed. First of all thanks to all of the fellow AMAC members for preparing the panels today. I thought they were very, very interesting.

I'll pick for comments on the ESG panel specifically and just four quick areas as the

subcommittee thinks about next steps, one around performance, another around factors themselves, disclosure, and then action.

On performance, I think it's -- we should tread cautiously on performance and tread cautiously about making claims that somehow ESG funds or firms are better or worse. It's really hard to keep that kind of thing a secret from the market. So if certain kinds of firms are really better or perform better that secret is going to get out and prices will get bit up, and it's very hard to imagine those kinds of things persisting. So on performance I would just from a committee perspective tread cautiously on any kind of statements we make about performance related to those factors. We would be wise to do that.

On factors I think what we're saying is ESG are characteristics or returns, so why bother to talk about them. That's one of the reasons the recent stock funds value momentum and size being characteristic of stock returns. So is the stock a value stock, is it a large stock, is it a momentum stock or not.

And a couple of things on that. One is those relative to ESG are very clear cut. You know, how much will your stock return, how big is it market cap wise. It's very hard to think about that kind of clarity in

the ESG factors. In addition, those change all the time. Sometimes value is booked to price, sometimes it's earnings to price, and letting the market sort itself out as to how it wants to define these factors, even returns, is it the best year, is it the best five years.

Over the last twenty or thirty years that -- those definitions have changed quite a bit and I think before we think about imposing standards on definitions of what E is, and what S is, and what G is we should be mindful given how even less hard to pin down they are than value, method and size, letting the market kind of figure what we mean by ESG is important.

On the topic of disclosure, I thought Commissioner Roisman made an important point. Companies are already required to disclose material risks, and I would just underscore that the market doesn't really hesitate to penalize firms that don't disclose material risks. They just -- the market does that pretty quickly. So I'd be careful in mandating disclosure, particularly because it could be misleading. If people think that they've got a disclosure around ESG risks but they just filled out a form and checked a box, we're actually going to lose information.

And then lastly on actions, you know, we're a

group of people around this committee where, quote, do nothing is -- it doesn't feel good. It's sort of not our natural state. But even if we chose to, quote, do nothing there's lot and lots and lots of stuff that's going on now in ESG.

And doing anything we have to remind ourselves we're basically encouraging the heavy hand of the state, the federal government, to bring down its standards on the whole country. That's a pretty high bar. And so I just don't think do nothing should be used pejoratively, I think it can be used not pejoratively. So I hope Michelle and the team take those comments onboard. I really appreciated the discussion.

MR. BERNARD: Thanks, really helpful thoughts. Russ.

MR. WERMERS: Thanks. I would be remiss if I didn't cite a couple of academic papers. So for the ESG panel, Jillian Grennan at Duke University has a paper that, empirical paper that points out that E and S and G kind be at odds with each other. For example you may have an independent, a very independent board that works hard for short term shareholder value and yet if we do so it costs an employee good wealth.

Another paper is a paper by Lubos Pastor from the University of Chicago with a couple of co-authors.

This is a theory paper, but I urge you to read it because it has some -- it has a lot of math in it, but it has some really great insights in there about that ESG might be thought of as a risk factor to hedge against.

And it says a lot to do with what Ross just said about this, is that ESG, heavy investments or investment funds may earn a lower raw rate of return but perhaps that's fair given that they're a hedge against future climate risks or just that they're preferred by investors, doing well is preferred by investors and they're happy to take this non-pecuniary benefit.

Fragmented investor, so of course I enjoyed that. I was still left wondering what, what are the panel's thoughts about mutual funds that hold more than 15 percent private investment, but not 100 percent, and think here my question was misunderstood. And I bring this up because I think given the dwindling pool of public, public securities it has to happen. I mean, defined contribution plans continue to grow. At some point funds are going to have to take on more private investments either through buying buildings, or investing in private equity funds, or whatever. So I was still left wondering, you know, are the risks that we've seen still applicable if the SEC

raises the threshold and mutual funds end up holding more of this along with their public securities as their liquidity buffer.

The final last thing, a plug for Gilbert. We're trying to settle on a date in November. I'm having a webinar on financial policy. I was so impressed with Gilbert last time that I'm holding a webinar with him in November. We're still working out the dates, I think, Gilbert. It will give me one more chance to hear you and to question you. Very well done.

MR. BERNARD: Thank you, Russ. Ryan.

MR. LUDT: Yeah, great. Thanks, Ed, and thanks again to all the committee members for the work that we've been getting done.

I think each of the committees or each of the panels were great today. From the subcommittees it's fantastic to see the D&I topic officially become a subcommittee and congrats to Gilbert and all those working on that.

Maybe two things that really seemed to emerge to me from the ESG and private investment were around transparency and education. So we heard it during the panels, and others here had mentioned it, I just think that has to be spinal to what we're doing as we continue that work is thinking about who are we educating, what

do they need to know, and how do we have transparency in that work as we go forward.

And on the D&I topic, I thought it was great to hear from both the consulting world and from the asset owner world. I think that gave us kind of a complete picture there.

And I think I've heard a few times throughout each of the sessions today that we do anticipate by, you know, December or the first quarter of next year to be looking to make more recommendations and do some more things. So back to that taking action I think it's fantastic to know that that's out there and we're getting to that stage in these topics. Because there's been a lot of thought and effort and getting those, getting those done will be fantastic.

MR. BERNARD: Great, thanks. Scot, Scot Draeger.

MR. DRAEGER: Thank you, Ed, and thank you to everyone who put work into today's presentations, they were all spectacular and very thoughtful.

Starting on ESG, a couple of things there. One, I'd be curious in the course of the work of the subcommittee to know how any recommendations that we might make relate and integrate with any global any standard setting that's going on in Europe or through

IOSCO or other bodies who have been considering these same issues.

I know that the Office of International Affairs at the Commission at the IOSCO bodies probably have a significant number of resources to draw upon, including some relationships. I guess I would just encourage that subcommittee to utilize those resources that are there.

Second, on the ESG, I think I -- we all share the hope that we can stem investor confusion in this area a little bit, and I think investor confusion or confidence with flow from truth in marketing and advertising as Joe hit on much more than it will from any details that we require in new prospectus disclosures.

So I would say to capitalize on that opportunity we're probably going to have to lean toward tightening up the nomenclature that is used, the broad use of ESG and SRI type terms in marketing and advertising rather than -- I think if we leave it to fund managers to have the latitude to define these terms however they want to interpret them, I think we will have missed an opportunity to reduce confusion by the retail investment community. So that's just my two cents on that.

The retail access to private investments, I would, I would agree with Erik Sirri that there was an opportunity here somewhere to get to a place where something appropriate is available to a retirement plan or other areas of retail access. I guess I would just say that at the moment, from everything that we've been educated on thus far, there seems to be more danger than there is a real taste that retailers really need access to this to round out their portfolio.

And I would -- I think we can't underestimate the liquidity needs. I mean, if you look at -- there are studies out there that show how much retail investors are using their investment funds for emergency healthcare funds and things like that. I think when we think in the context of some of the liquidity needs of mainstream investors, you know, those are, those are real things to consider.

And then the average 401(k) plan sponsor doesn't have access to the Hamilton Lanes and the Cambridge firms of the world. Those firms are obviously the most, among the most reputable sources of due diligence in the world, but I think we have to be realistic about the segments of the market, which is about 95 percent, that will never have access to that level of diligence.

So -- and then finally I just want to say, Gilbert, you just inspire the heck out of me. I mean, just every time you're here and what you're putting together I'm so excited to be in this with you. Today we focused on the asset aggregators and allocators. I think, you know, as we've talked about a little bit before the vast majority of firms are serving individual families with sometimes individual stocks and bonds. So I'm excited to get to the place where we figure out how we encourage diversity as a value among those firms in addition to the asset aggregators of the world.

Thank you, Ed.

MR. BERNARD: Thank you. Susan McGee.

MS. McGEE: I'd like to thank the committees today as well. They did a phenomenal job.

I was very pleased with the ESG panel and their slide presentation and balancing out pros and cons with different stages of proposals. I'm very cautious about throwing regulations out there as, hopefully as a cure all because they do have a lot of costs and they are -- they can be very burdensome.

So I realize that something needs to be done with the confusion and the clarity on ESG. I just hope that we as a committee focus on recommending something that's very efficient and keep an eye on the cost and

the burdens that any recommendation might have.

And then the other comment I had was on diversity and inclusion. You know, we -- this is a good idea, it's a good thing that we all, you know, as a society need to embrace. We talked at the last meeting about how do we translate this into a possible recommendation to the SEC.

There were two comments that came out of the panel today that I thought really spoke to us as a panel. I've enjoyed that. One of them was teaching or teaching your underwriters how to look at smaller managers since these diverse management firms tend to be smaller, I thought that was really good, and also hiring personnel within, more of a grassroots, you know, approach to things.

However, I really enjoyed the Illinois Treasurer because he did give us some, some points to consider. Do we want -- are these things that we would like to recommend to the SEC, is it something that the SEC, you know, can tackle or is this best left to, you know, to other avenues.

But those were my comments for today.

MR. BERNARD: Great. Last time I missed somebody, I think it was Ryan that I missed last time with the way the lists were kept. Have I missed anybody

today or did we get everybody? Great.

And Jane, I assume we still can't hear you, so I'm going to let you go. I'm not sure what happened, so I won't go back.

I guess it does come to me. I'm going to have a slightly different reaction. I'm not going to try and add to all the insights that everyone just shared about the presentations. I actually want to react to today and just say I continue to be humbled by the talent of this group. I thought everything we saw and heard today was just of the very highest quality. We're dealing with some really complex issues, and you're taking on the complexity head on, and I'm -- in addition to that humility I'm grateful for the -- there's an enormous amount of work that goes into all this and will continue as everyone can tell with what these teams are taking forward.

So I'm grateful for that and to the point that was just made about getting to action, I think we're getting there. We just did our first formal recommendations today. I think we'll see some more within a month's time and we'll start to see more even in December.

So with that I just want to thank everyone for your participation today. I know it's a long day on a screen. I think it was an extremely valuable day and thank all the subcommittee leaders, the members, and those who put together the panels today.

And with that I will turn to Dalia to see if you would like the last word.

MS. BLASS: Yes. And cognizant of the fact that I'm in between you and getting away from your screens and have a few words, but just a few things.

One is there were five very distinct topics and each one of them extremely complicated. And, you know, the presentations have the tradition of very thoughtful, very thorough presentations. And the panelists that you all invited today, they were subject matter experts. Their presentations were data driven and they shared their experiences. All the subcommittees, you know, you shared with us, like, a framework for how you're approaching your work, which is extremely helpful.

I also would like to commend the AMAC for taking on diversity and inclusion as a formal subcommittee. It's a critical issue for the asset management industry and society as a whole. And I also, and Gilbert your enthusiasm, your energy through the panel is just truly, truly amazing. I'm looking forward to the work, you know, from the subcommittee.

Michelle and the ESG subcommittee, I thought your initial, you know, lead in May was just really extraordinary. I was -- today you even stepped it up more. The presentation, what you -- how -- the framework that you guys have laid out I'm really interested in seeing where you take it.

Particularly for me I was really interested in your analysis in the names rule and the value versus values. I thought that was really laid out in a very interesting format.

I will say that as you consider your work in this area one thing to also keep in mind is that, you know, it's not work in a vacuum. There are other participants in this conversation. For example in Europe there is a tremendous amount of work going on there at the regulatory level in terms of sustainable finance and work in other jurisdictions because of the global nature of the asset management industry as of now does tend to come into our issues faced today and tomorrow. So something to keep in mind as you continue that work on the different areas that you're exploring.

For that -- one other thing that really struck me is the ESG for the private access and for diversity and inclusion is how data driven, you know, the areas are and frankly also the lack of data. So something --

you know, as much as the presentations were all data driven, every single one of them also reflected the lack of data and the importance of data. So something that really kind of was really a takeaway for me is to what extent we do need more data.

And finally on the operations workstream, very, very thoughtful presentation. I will say, you know, could have ever anticipated the operational challenges and the posture that we're all in today. Technology has been amazing. I mean, look at what it's enabled us to do today, but also today by the way look at all the technological issues that we have faced. So there are pros and there are cons. It can do so much, but it does -- it may have shortcomings here and there. So something that, you know, just to keep in mind as we sort of, you know, go forward in this but really critical areas that perhaps had not risen to the forefront really have become really important for us to sort of think about and move forward.

I would just add, I hate to add to your list because it was a very fulsome list, but one thing perhaps to take into consideration as technology becomes more important is the cyber risk. It really adds something that will just be fundamental to any technology. Cyber risk is something that I just kind of

wonder if you had thought about that, if that's something you would explore.

So I know that's a lot, but I was trying to get it through pretty quickly so that you can close out. But thank you again for your time, for all the work that you are doing and continuing to do. For all the subcommittee heads, amazing presentations. And for the ETFs and the operations workstreams, thank you for that. I mean, this was -- operations workstreams, you guys put together quickly how the recommendations were put in ETF, truly, truly amazing work and thank you, appreciate it. Ed.

MR. BERNARD: Great. Thank you, Dalia. That was really helpful input.

With that I was hoping -- I'm going to give you back nine minutes. We were due to finish at 4:15. I'm -- it's important to me to finish on time and if we can finish early that's great.

Be on the lookout for -- well, you may see some follow up notes from me or subcommittee leads seeking feedback and input. We always appreciate your being attentive to those.

You will likely see a request from the SEC team looking for a, what I think will be a very brief meeting sometime in, I'm going to say October timeframe, but let's just call it fall, to follow up on Mike Durbin's discussion.

The next full day meeting is scheduled for Tuesday, December 1st. I hope everybody has that marked in your calendar. And with apologies, although we all responded with the dates, that's the Tuesday after the week of Thanksgiving.

So in any case, thanks again to all of our speakers and leaders and to all of your participation and have a great day. My screen is flashing red and my screen time is over for the day, so I'm going to turn it off. Thanks everybody.

(Whereupon, at 4:07 p.m., the meeting was adjourned.)

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PROOFREADER'S CERTIFICATE

In the Matter of: ASSET MANAGEMENT ADVISORY COMMITTEE MEETING

File No: OS-0916

Date: Wednesday, September 16, 2020

Location: Washington, D.C.

This is to certify that I, Christine Boyce (the undersigned), do hereby certify that the foregoing transcript is a complete, true and accurate transcription of all matters contained on the recorded proceedings of the meeting.

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I, Kevin Carr, reporter, hereby certify that the foregoing transcript is a complete, true and accurate transcript of the matter indicated, held on __9/16/2020___________, at Washington, D.C., in the matter of:

ASSET MANAGEMENT ADVISORY COMMITTEE MEETING.

I further certify that this proceeding was recorded by me, and that the foregoing transcript has been prepared under my direction.

9/17/2020

Kevin Carr

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