

D&I Developments at the SEC - Part 1 of 2

In recent weeks two important regulatory developments focused on diversity and inclusion (D&I) have come out of the SEC: the D&I Subcommittee of the SEC's Asset Management Advisory Committee (AMAC) presented and received approval for its [recommendations](#), and the SEC issued an [order](#) approving rule changes proposed by The Nasdaq Stock Market LLC (Nasdaq) relating to board diversity. SEC Chair Gary Gensler and other commissioners have publicly supported the Subcommittee's recommendations and the new Nasdaq rules. But these developments are not uniformly popular at the SEC. **D&I Subcommittee Recommendations** The D&I Subcommittee's recommendations follow significant research and study that the subcommittee says yielded "quantitative data on the lack of diversity and inclusion, the qualitative 'human' side of experiences shared by women and people of color in the industry, and the call by investors for more transparency on diversity." Among the Subcommittee's findings were that:

- active discrimination exists and remains a barrier for minority- and women-owned firms;
- women and people of color "remain dramatically underrepresented" within asset management firms and fund complexes;
- investment performance by diverse asset managers is clearly "equal to or greater than the investment performance of firms that lack diversity in ownership and senior leadership, despite differences in size and length of track record;" and
- "diverse perspectives, diverse work forces, diversity of those who have access to capital" and increased diverse ownership within the asset management industry are each in the "public interest."

Noting that it had focused on identifying areas where increased transparency on D&I matters would be "material" to an investor's selection of an investment adviser or investment fund, the Subcommittee put forth the disclosure and other recommendations described below. *Disclosure Recommendations for Funds and Advisers*

- Mutual funds should be required to provide registration statement disclosure on the gender and racial diversity of the fund board and the adviser's and any sub-adviser's workforce, management, and ownership;
- Investment advisers should be required to provide Form ADV disclosure on gender and racial diversity in the firm's workforce, management, and ownership; and
- Advisers that recommend third-party funds and advisers should be required to provide disclosure on their consideration of diverse asset management firms.

Guidance on Selection of Diverse Firms

- The SEC should "encourage the use of diverse managers in order to promote the best outcomes for investors" and should provide guidance clarifying that an adviser's fiduciary duties do not prohibit it from recommending to clients asset managers "who are newer to the industry or do not already have a certain level of AUM," such as many diverse asset managers.

Pay-to-Play

- The SEC should study whether the current Advisers Act pay-to-play rules allow "disproportionately large, nondiverse, firms" to make political contributions and procure influence through PACs while smaller

and/or diverse asset management firms are restricted in their political contributions, "contrary to the spirit of the pay-to-play rules."

Reports of Discrimination

- The SEC should: establish a system for referring reports of discrimination to an appropriately equipped government office; catalogue and maintain records of such reports "in a manner that can be evaluated over time;" and publish a list of resources for victims of discriminatory practices in the asset management industry.

Commissioners' Remarks In [his opening remarks](#) at the AMAC meeting, Chairman Gensler expressed agreement that "the asset management industry has a lot of work to do to increase racial and gender diversity" and said that he had asked staff to consider ways to enhance the transparency of D&I issues in the industry. In [her opening remarks](#) before the meeting, Commissioner Hester Peirce raised a variety of concerns around "government-mandated diversity classifications" and asked, among other questions, how the SEC would define "diversity," what an asset manager would do "if an employee or board member prefers not to identify her ethnicity or gender," and how the SEC would verify firms' statements of diversity. **Conclusion** The subcommittee's recommendations have generated significant buzz in the industry as asset management firms continue integrating D&I considerations into their overall ESG messaging and related compliance policies and procedures. CCOs should work with counsel as necessary to ensure that D&I disclosures are supported by accurate documentation and otherwise comply with the guidance included in the SEC's April 2021 [ESG risk alert](#). In Part 2 of this post, we'll discuss the new Nasdaq board diversity rules and what the SEC Commissioners have to say about them.

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