

Via Hand Delivery

November 25, 2019

The Honorable Maxine Waters
Chair
Committee on Financial Services
United States House of Representatives
Washington, DC 20515

The Honorable Patrick McHenry
Ranking Member
Committee on Financial Services
United States House of Representatives
Washington, DC 20515

*Re: November 19, 2019 hearing entitled, "America for Sale? An Examination of the Practices of Private Funds"*¹

Dear Madam Chair and Ranking Member McHenry:

I am writing on behalf of the Council of Institutional Investors (CII) to express our appreciation to you for holding the above referenced hearing and to provide you with our views on private equity funds, including our general support for one of the draft legislative proposals discussed at the hearing. We would respectfully request that this letter be made a part of the hearing record.

CII is a nonprofit, nonpartisan association of U.S. public, corporate and union employee benefit funds, other employee benefit plans, state and local entities charged with investing public assets, and foundations and endowments with combined assets under management of approximately \$4 trillion. Our member funds include major long-term shareowners with a duty to protect the retirement savings of millions of workers and their families. Our associate members include non-U.S. asset owners with about \$4 trillion in assets, and a range of asset managers with more than \$35 trillion in assets under management.²

Private Equity Funds

Private equity funds play a significant role in the economy as a source of capital, as an investment vehicle, and as a growing job provider. For many of our member funds, private equity provides the asset diversification that those funds require to meet their fiduciary

¹ *American for Sale? An Examination of the Practices of Private Funds, Before the H. Comm. on Fin. Servs., 116th Cong.* (Nov. 19, 2019), <https://financialservices.house.gov/calendar/eventsingle.aspx?EventID=404650>.

² For more information about the Council of Institutional Investors ("CII"), including its board and members, please visit CII's website at <http://www.cii.org>.

obligations to their beneficiaries.³ However, CII has long held the view that private equity funds should provide disclosures that:

[F]oster transparency and accountability throughout the capital markets, thus enhancing confidence in the markets. They would also . . . guard against misuse of fund assets and abuses of the power inherent in large pools of capital.⁴

We continue to support improvements to the disclosures provided by private equity managers to member funds, including fee and expense reporting. We generally agree with the testimony of hearing witness Wayne Moore, Trustee, Los Angeles County Employee Retirement Association, that “better industrywide information from private equity firms on fees, expenses and returns is needed to ensure the proper alignment of interests is realized.”⁵ We also generally believe that better disclosures are critical to ensuring that investment contracts signed by our member funds are complied with by the private equity managers.⁶

H.R. _____, the Investor Adviser Alignment Act (Alignment Act)⁷

CII generally supports the Alignment Act. We note that the provisions of the Alignment Act include defining private equity advisor and requiring private equity investors be provided with Securities and Exchange Commission (SEC) filings, quarterly reports of fees and expenses, and all information related to an SEC examination, inquiry, or enforcement action.⁸

We are particularly supportive of the provisions of the Alignment Act requiring quarterly reporting of all fees and expenses.⁹ We generally agree with the views of the Institutional Limited Partners Association that:

The lack of fee and expense transparency in the marketplace as an issue became apparent soon after the SEC began examining GPs. In 2014, the SEC indicated after

³ See, e.g., Letter from Ashbel C. Williams, Executive Director & CIO, State Board of Administration of Florida, to The Honorable Maxine Waters, Chairwoman, Committee on Financial Services, U.S. House of Representatives et al. 1 (Nov. 19, 2019) (on file with CII) (“Private equity provides necessary returns and asset diversification that the SBA requires to meet our fiduciary obligations to our beneficiaries.”).

⁴ See, e.g., Investors’ Working Group, *U.S. Financial Regulatory Reform: The Investors’ Perspective* (July 2009), https://www.cii.org/files/issues_and_advocacy/dodd-frank_act/07_01_09_iwg_report.pdf. Following its issuance, the IWG Report was reviewed and subsequently endorsed by the Council board and membership. For more information about the Investors’ Working Group, please visit the Council’s website at https://www.cii.org/investors_working_group.

⁵ *American for Sale? An Examination of the Practices of Private Funds, Before the H. Comm. on Fin. Servs.*, 116th Cong. (Nov. 19, 2019) (Written Testimony from Wayne Moore, Trustee, Los Angeles County Employee Retirement Association at 1), <https://financialservices.house.gov/uploadedfiles/hhrg-116-ba00-wstate-moorew-20191119.pdf>.

⁶ See, e.g., Letter from Dan M. Slack, Executive Director, Fire and Police Pension Association of Colorado to The Honorable Maxine Waters, Chairwoman Committee on Financial Services, U.S. House of Representatives et al. 1 (Nov. 18, 2019) (on file with CII) (“We also actively seek fee and expense reporting from the private equity managers we invest with and find it critical to ensure the investment contract we signed with the GP is complied with.”).

⁷ H.R. _____, the Investment Adviser Alignment Act, 116th Cong. (2019) (Discussion Draft), <https://financialservices.house.gov/uploadedfiles/bills-116pih-iaaa.pdf>.

⁸ *Id.* § 2(a)-(b), (d)-(e).

⁹ *Id.* § 2(d).

their initial round of 150 examinations that “[w]hen we have examined how fees and expenses are handled by advisers to private equity funds, we have identified what we believe are violations of law or material weaknesses in controls over 50% of the time.” A 2016 speech by then-SEC Division of Enforcement Director, Andrew Ceresney further highlighted the transparency challenges around costs facing LPs: “[I]nvestors in certain circumstances do not have sufficient transparency into how fees and expenses are charged to portfolio companies or the funds. Sometimes fees are not properly disclosed, conflicts are not aired, expenses are misallocated, and investors are defrauded... even experienced [and sophisticated] investors can be defrauded if they lack transparency into the various fees, expenses and practices.” As LPs became more aware of these issues in the industry, they needed a solution to ensure they could verify the fees and expenses they were being charged.

. . . Given the complexity of the fees and expenses charged to the fund and to portfolio companies, quarterly fee and expense reporting is critical to investors and must be included in any reform seeking transparency in private equity.¹⁰

If we can answer any questions or provide additional information that would be helpful to you or the Committee, please do not hesitate to contact me at 202.822.0800 or jeff@cii.org.

Sincerely,



Jeffrey P. Mahoney
General Counsel

¹⁰ Letter from Steve Nelson, Chief Executive Officer, Institutional Limited Partners Association, to The Honorable Maxine Waters, Chairwoman, Committee on Financial Services, United States House of Representatives 3-4 (Nov. 18, 2019), <https://ilpa.org/wp-content/uploads/2019/11/ILPA-Letter-for-the-Congressional-Record-on-Nov.-19-2019-HFSC-Hearing.pdf> (footnote omitted).