

October 17, 2022

SEC Staff Issues FAQ Regarding Investment Adviser Consideration of DEI Factors

On October 13, 2022, the SEC staff [published](#) a single FAQ and response (the “Staff Guidance”) confirming that, consistent with its fiduciary duty and subject to certain conditions, an investment adviser can incorporate diversity, equity and inclusion (“DEI”) factors when recommending or selecting an investment adviser for its clients. Specifically, the Staff Guidance stated:

Q. Under its fiduciary duty, may an investment adviser that recommends other investment advisers to or selects other advisers for its clients consider factors relating to diversity, equity and inclusion, provided that the use of such factors is consistent with a client’s objectives, the scope of the relationship, and the adviser’s disclosures?

A. Yes. An investment adviser is required to have a reasonable belief that the advice it provides is in the best interest of the client based on the client’s objectives. Such a reasonable belief that advice is in the best interest of the client typically includes consideration of a variety of factors.

Accordingly, an adviser that recommends other investment advisers to or selects other advisers for their clients may consider a variety of factors in making a recommendation or selection, including, but not limited to, factors relating to diversity, equity, and inclusion, provided that the use of such factors is consistent with [i] a client’s objectives, [ii] the scope of the relationship and [iii] the adviser’s disclosures.¹

Commissioners’ Statement

On the same day as the publication of the Staff Guidance, SEC Commissioners Crenshaw and Lizárraga published a related joint [statement](#) (the “Statement”). The Statement noted that the Staff Guidance was issued in response to the 2021 Asset Management Advisory Committee (the “AMAC”) report and its recommendations to the SEC on diversity and inclusion, “addressing the ‘well-known and widely acknowledged’ lack of gender and racial diversity in the asset management industry.”

The Statement also noted that the AMAC report contained recommendations intended “to shine light on potential discrimination and barriers to women and minorities in the industry, and to provide transparency around diversity practices and data, which carry considerable weight with investors.” However, the Statement highlighted, “as the AMAC report stated, ‘its focus was on disclosure, not on mandating any business decisions or practices by SEC registrants.’”

Observations

The Staff Guidance provides greater certainty to investment advisers seeking to incorporate DEI factors when recommending or selecting an investment adviser for clients. Although the Staff Guidance makes no express reference to registered funds, it would appear to apply with respect to all such recommendations and selections, including those involving the selection of sub-advisers by advisers to registered funds that operate in a manager-of-managers structure. In such instances, an investment adviser may want to consider, in addition to its Form ADV and other disclosures, disclosures to fund shareholders.

1. The Guidance cautioned that investment advisers also subject to regulation by the U.S. Department of Labor “should consider such applicable laws and regulations when providing advice.”