HOW THE PRIVATE EQUITY INDUSTRY NEEDS TO IMPROVE WHEN ADDRESSING SYSTEMIC AND SYSTEMATIC RISKS

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CREDITS

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Dmitriy sits at the center of the conversation around ESG and impact investing, helping different stakeholders communicate with their target audiences and develop a shared understanding of goals, needs and challenges. As the lead author of the ‘Private Inequity’ report, Dmitriy designed the research study, evaluated the research results and wrote the bulk of the report with input from the rest of the team.

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DELILAH ROTHENBERG is the Founder and Executive Director of the Predistribution Initiative (PDI), a multi-stakeholder project to co-create improved investment structures focused on mainstream markets with risk-adjusted returns that share more wealth with workers and communities, have stronger investment team incentives for ESG integration, and address systemic and systematic risks including inequality and climate change. Underpinning this work is research on how to more adequately pay people for the value they create and risk that they take throughout the “capital markets value chain” (investee workers and management, individuals within the asset manager, the asset owner/allocator), as well as structuring incentives for longer-term outlooks, and the potential for more inclusive models of governance. Since 2009, Delilah has also advised private equity investors, lenders, and project developers on ESG and impact through Development Capital Strategies (DCS). Prior to 2009, Delilah focused on institutional equities with Bear Stearns and Gerson Lehrman Group (GLG).

As a contributing author on the ‘Private Inequity’ report, Delilah contributed to the framing of the issues, as well as the ‘Recommendations’ section with details on specific actions that private equity firms can take to address systemic and systematic risks.
ACKNOWLEDGEMENTS

We would like to thank the multi-disciplinary and diverse team that was involved in the making of this report. We intentionally sought to bring together a diverse set of viewpoints in attempt to capture the full breadth and depth of the systemic crises discussed in this report.

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In a world of growing systemic risks, including inequality and climate change, we may be at a pivotal moment for finance in the struggle to build a truly sustainable and equitable society. But how do we get there?

Many people think about stocks, bonds, and banks when the words “investing” or “finance” are mentioned. But did you know that stock markets are shrinking, now less than half of their late 1990’s peak? At the same time, private markets are growing. A 2020 McKinsey report notes that global private equity “…net asset value has multiplied eight times since 2000, almost three times as fast as public market capitalization.” In the United States, the number of private equity-backed companies doubled from about 4,000 in 2006 to 8,000 in 2017. Private capital (including private debt, venture capital, infrastructure, real estate, etc.) assets under management (AUM) is now approximately US$6.5 trillion – an increase of over US$4 trillion in the past 10 years.

The growth of private equity ownership of companies in the global economy has significant implications for workers and communities. Estimates of Americans employed by private equity-backed firms range from nearly nine to 11 million people. And private equity firms now have a strong presence in sometimes essential and sometimes controversial industries including healthcare and hospitals, nursing homes, housing, infrastructure, and even private prisons and security.

To many, the increasing influence of private equity has understandably been concerning, particularly given the historical lack of transparency in the industry and the risk that certain investment structures and strategies can potentially contribute to inequality. On the other hand, private equity firms often take controlling governance positions in their portfolio companies and can influence the capital structures. As such, they are well-positioned to push for positive changes in the companies they manage—if they so choose.

As investors continue to allocate more capital to this asset class, it is critical that the industry self-reflects on what practices it might have adopted that contributed to our current state fragility, and what it can do to change for the “better.” Importantly, this self-reflection cannot happen in a vacuum if we are truly committed to living in an era of “stakeholder capitalism,” when organizations from the World Economic Forum to the Business Roundtable are acknowledging the need to engage all stakeholders, not just shareholders.

The private equity industry can shift to become an important part of the solution, but we need improved transparency and accountability if we are going to trust their efforts to Build Back Better. Recent controversies about the industry’s role in weakening corporate balance sheets at the expense of workers, concentrating wealth in the hands of executives, and deteriorating the quality of essential goods and services have collectively eroded public trust. And yet, private equity firms, with their strong ability to influence governance and shape investment structures, are uniquely positioned to play an important role in improving the shape of capitalism.

Right now, private equity firms are stuck in a ‘one step forward, two steps back’ mindset. But incremental solutions will not generate progress if we leave systemic and systematic risks unchecked. We need structural change and systemic reform, both within the private equity industry, as well as in our larger society. Private equity firms, with their vast financial resources and intellectual capital, can help lead the way towards a true stakeholder capitalism model. The private equity industry can function as a staging ground for the rest of the capital markets, given its unique features and growing influence. Practices that are adopted by private equity firms can
set a positive example for other types of asset management firms. We still have a chance to get this right and break the cycle of incrementalism. A “better” future where systemic and systematic risks are managed, rather than ignored, is at our grasp.

DEILAH ROTHENBERG

FOUNDER & EXECUTIVE DIRECTOR OF
THE PREDISTRIBUTION INITIATIVE
EXECUTIVE SUMMARY

INTRODUCTION

Are private equity firms doing enough to address systemic and systematic risks at their root, or are they offering mere platitudes in response to crises and then returning to business as usual? According to Investopedia, “Systemic risk describes an event that can spark a major collapse in a specific industry or the broader economy. Systematic risk is the pervasive, far-reaching, perpetual market risk that reflects a variety of troubling factors. Systemic risk is often a complete, exogenous shock to the system, such as the threat that one of the major banks that collapsed during the 2008 financial crisis could then trigger a massive market implosion. Systematic risk is the overall, day-to-day, ongoing risk that can be caused by a combination of factors, including the economy, interest rates, geopolitical issues, corporate health, and other factors.” See https://www.investopedia.com/ask/answers/09/systemic-systematic-risk.asp for more information.

This important question inspired our research, which was designed to evaluate how 100 of the biggest private equity firms are publicly responding and reacting to the growing list of crises that continue to proliferate around the world.

Over the past year in particular, the world has encountered three distinct, yet interconnected crises that attracted international media attention and an outpouring of public statements and donations in support. These crises are also similar in that they disproportionately affected low-income communities and those who are Black, Indigenous, or People of Color (BIPOC). The three crises we reference include:

- **CLIMATE CHANGE**, as highlighted by bushfires in Australia, wildfires in the Amazon and western United States, and other major recent climate events

- **COVID-19 PANDEMIC**, which illuminates the shared fragility within our socioeconomic and financial systems

- **RACIAL INJUSTICE**, as highlighted by the Black Lives Matter (BLM) movement and the mass protests against longstanding and persistent systemic racism and police brutality
Each of these crises are manifestations of systemic risks that are well-known, yet continue to be ignored, underfunded or inadequately addressed by both the public and private sectors. And while governments, businesses and philanthropies are actively seeking to respond to these crises and support those who are most affected, we need to look at the root causes of the systemic issues that create these risks in the first place – many of which are intertwined in the very plumbing of the financial system on which our economy operates.

Far from being “black swans,” these crises were each anticipated years in advance and could have been prevented or mitigated with strong proactive action, particularly from the private sector. The failure to act has resulted in untold human suffering and increased costs for virtually everyone – investors, companies, governments, and civil society alike.

Private equity firms in particular have an increasingly important role to play in addressing these risks due to their growing influence over the economy, especially as owners of thousands of businesses employing millions of people (see the Foreward for additional data). Such risks manifest in financial markets in the form of systematic risks, which eventually boomerang back to investors and damage the financial performance of their portfolios.

Private equity firms, armed with $1.5-$2.5 trillion in dry powder, are now poised to augment their control over a bigger share of the global economy, especially with so many businesses starved for cash in the wake of an economic crisis that shows no signs of abating.

However, we found that the communications playbook used by most private equity firms follows the “thoughts and prayers” model—obligatory statements suggesting empathy, but with little commitment to tangible, self-reflective action to prevent a recurrence of the same problem or issue.

CONTINUED

Our research backs up this conclusion. In preparing this report, we evaluated a total of 2,400 potential responses that PE firms could have made—eight responses per each of the three crises for 100 firms (or 800 responses per crisis). These responses included issuing a public statement, making a donation, announcing internal changes (e.g., hiring practices, training practices, reporting practices) or committing to external changes (e.g., engaging with portfolio companies on Environmental, Social, and Governance (ESG) issues, aligning investment and incentive structures with ESG integration and / or outcomes, aligning lobbying and political spending with ESG goals). However, in total we only found evidence for 264 responses, suggesting significant room for improvement.

In the remainder of this report, we discuss these different types of responses in more detail, analyze how private equity firms responded to the three crises discussed, and offer a list of suggested recommendations to achieve systems change.

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7 We note there is potential for lobbying and political spend to have been considered a type of internal change, and reporting and disclosure could have been a type of external change. Despite this, their placement in their current categories do not change the resulting numerical analysis presented in this report.
Using a combination of quantitative and qualitative analysis, we designed a research study to get at the heart of how some of the most active private equity firms are responding to these crises and whether they are taking steps to address root causes.

**SAMPLE SIZE**

We analyzed the 100 private equity firms that had raised the most capital over the previous five years, according to rankings published by Private Equity International in Q1 2020. The majority of these firms (70%) are based in the U.S. and collectively manage more than US$1 trillion.

**EVALUATION CRITERIA**

We looked at two different types of responses – non-systemic responses that are unlikely to move the needle, and systemic responses that have the potential to create long-lasting change. We defined two categories of non-systemic responses: public statements and donations. And we defined six categories of systemic responses, including three potential internal changes to how private equity firms manage their business and three potential external changes to how private equity firms manage their investments. In total, we looked at eight categories or potential types of responses (all of which were non-mutually exclusive). [See Fig. 1]
## Evaluation Criteria

<table>
<thead>
<tr>
<th>Type of Response</th>
<th>Categories</th>
<th>Examples</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Non-Systemic Responses</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Public Statement: A private equity firm acknowledging that there is a problem by issuing a statement about a particular cause or issue</td>
<td>N/A</td>
<td>Publishing a ‘letter from the CEO’ or a short statement on social media</td>
</tr>
<tr>
<td>Donation: A private equity firm “giving back” to non-profits working to address one or more of these issues by making a donation and/or announcing an employee match program</td>
<td>N/A</td>
<td>Announcing a donation to one or more non-profits or non-governmental organizations; announcing an employee match program</td>
</tr>
<tr>
<td>Internal Change: A private equity firm self-reflecting on how its internal practices may be contributing to certain problems and/or how it discloses essential information to both internal and external stakeholders</td>
<td>(1) Hiring &amp; procurement practices</td>
<td>(1) Hiring more climate or ESG professionals; ensuring diverse representation at all levels of the organization and developing supportive policies and procedures; committing to pay equity; improved recruiting and procurement practices (e.g., intentionally seeking out diverse team members and vendors); etc.</td>
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<td></td>
<td>(2) Employee training &amp; resources</td>
<td>(2) Forming ESG committees; organizing racial sensitivity and Diversity, Equity, and Inclusion (DEI) trainings; instituting grievance mechanisms according to international human rights standards; modifying agreements that otherwise limit redress of grievances (e.g. forced arbitration and certain non-disclosure provisions); implementing work-from-home and leave policies; etc.</td>
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<tr>
<td></td>
<td>(3) Public reporting &amp; disclosures</td>
<td>(3) Publishing ESG or sustainability reports with supporting data and evidence; reporting in alignment with industry standards; disclosing diversity and pay ratio breakdowns and targets; etc.</td>
</tr>
<tr>
<td><strong>Systemic Responses</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>External Change: A private equity firm acknowledging its role relative to these systematic risks and making changes to its investment strategy, portfolio management, team incentive structures and performance reviews, and/or fund and investment structures</td>
<td>(1) Investment strategy &amp; portfolio engagement</td>
<td>(1) Investing in more sustainability-oriented companies and/or companies with diverse leadership; creating exclusion lists or moving mandates away from risky sectors (e.g., fossil fuels, private prisons, etc.); supporting portfolio companies in addressing ESG issues (e.g., job quality) and transitioning to more sustainable business models; etc.</td>
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<td></td>
<td>(2) Investment structures &amp; aligning incentives</td>
<td>(2) Aligning staff incentives with ESG integration or impact outcomes; implementing more regenerative investment structures; maintaining reasonable leverage ratios; improving tax transparency and responsibility; narrowing pay ratios between the average portfolio company worker and fund manager executives; etc.</td>
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<tr>
<td></td>
<td>(3) Political spending &amp; engagement</td>
<td>(3) Aligning lobbying and political spend practices with stated ESG goals; disclosing all political spending at the fund manager level and, where feasible, the portfolio company level; etc.</td>
</tr>
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9 Examples of standards and guidelines include, for instance,: Sustainability Accounting Standards Board (SASB), Global Reporting Initiative (GRI), Impact Management Project (IMP), Principles for Responsible Investment (PRI), IRIS+, Sustainable Development Goals (SDGs) and the Task Force on Climate-related Financial Disclosures (TCFD).

The non-systemic responses (e.g., statement OR donation) are high-level responses to problems, versus adjustments to the roots of such problems. Thus, they are not transformational. In contrast, the six different types of systemic responses represent important steps in the direction towards transformational systemic and systematic change. That is, the non-systemic responses will not be successful if the latter two issues go unaddressed and continue to exacerbate problems. It is also worth noting that the systemic responses will also not be effective without the appropriate policies, procedures, responsible parties, communication and training, and transparency and accountability mechanisms needed to ensure implementation. We describe these elements further in the ‘Recommendations’ section of this report on page 28.

**DATA COLLECTION**

The research team reviewed ONLY publicly available information published by a private equity firm (or about a private equity firm) between June 2019 and July 2020 (the ‘Research Period’). This information was sourced from a combination of corporate websites, social media channels and news articles. Any public statements or commitments must have been made by Friday, July 10, 2020 in order to be included in the research. The research was conducted over two rounds, which means each private equity firm was evaluated by two different researchers to provide an additional quality check. Researchers spent 30 minutes looking at each firm, which we believe represents a reasonable amount of time needed to find the necessary information. It is certainly possible that we missed some publicly available information about responses or commitments by firms in the sample. However, our rationale is that if it was that time-consuming to locate the information, then it was poorly communicated, which is effectively the same as not being communicated in the first place.

We intentionally only looked at NEW announcements or initiatives that were disclosed during the Research Period. Having worked inside the private equity industry and in our ongoing interactions with private equity professionals, we recognize that private equity firms have made some progress in addressing these issues. For example, some have taken steps to conduct TCFD assessments, invest in circular economy solutions, support portfolio companies and
society during times of crisis, or improve DEI in their investment teams and portfolio companies. However, these announcements have been sparse and few and far between. Furthermore, many of these same firms continue to invest in fossil fuels alongside renewables and/or have taken retaliatory steps against portfolio company workers concerned about their health and safety, and we are far from making the progress needed to incorporate more diversity into investment decisions.

Private equity firms need to take a more comprehensive and systemic approach. Part of the challenge is that private equity firms generally lack real policies and procedures with targets and timelines that can be used to reach specific goals. Another challenge is that it is impossible to hold private equity firms accountable on these goals if there isn’t communication about progress or results, which we believe should happen regularly.\footnote{Pucker, Ken, and Sakis Kotsantonis. “Private Equity Makes ESG Promises. But Their Impact Is Often Superficial.” Institutional Investor, 29 June 2020, www.institutionalinvestor.com/article/b1m8spzx5bp6g7/Private-Equity-Makes-ESG-Promises-But-Their-Impact-Is-Often-Superficial.}

Our intent in this report is not to punish firms that are already taking tangible steps. We are not here to pick winners or losers, which is why we have chosen not to name any particular firms or provide specific examples of actions taken. Rather, our goal is to take an industry-wide approach to advance best practices in an asset class that many believe is already behind the curve, but has strong potential for systems change.

**ANALYSIS**

Every time we found a public statement, quote or disclosure that fit into one of our eight categories (e.g., statement, donation, three internal changes, or three external changes), we credited that firm with ONE point. Firms could not earn multiple points per category per crisis. For example, if a firm made multiple statements in response to COVID-19, that would still only count as one point. However, if a firm made a statement in response to both COVID-19 and climate change, then that would count as two points.
This research could and should be expanded to other sectors of the asset management industry. However, we decided to focus first on private equity because of the increasingly significant role that private equity firms play in the global economy. Global assets under management for private equity have surged above US$5 trillion, with approximately US$1.5—2.5 trillion in uncalled capital, or “dry powder.” Private equity firms control an estimated 8,000+ businesses in the U.S. and are responsible for 5% of the GDP (approximately US$600 billion in wages and benefits) and a significant share of the workforce (26 million American jobs, when including indirect jobs). As we enter what may be a prolonged downturn, private equity firms stand poised to use their dry powder (potentially combined with cheap debt due to low interest rates) to acquire distressed assets. The prospect of opaque investment firms with significant power and questionable ESG track records owning more and more of our economy may sound ominous. On the other hand, private equity firms, many of whom have large equity stakes and representation on company boards, wield much more influence on their portfolio companies than other types of investors employing a public equity or fixed income strategy. As such, private equity firms are among those best positioned in the asset management industry to enact positive systemic change.

**FAQ**

**Q** WHY IS THE RESEARCH FOCUSED SPECIALLY ON THE PRIVATE EQUITY INDUSTRY?

**A** This research could and should be expanded to other sectors of the asset management industry. However, we decided to focus first on private equity because of the increasingly significant role that private equity firms play in the global economy. Global assets under management for private equity have surged above US$5 trillion, with approximately US$1.5—2.5 trillion in uncalled capital, or “dry powder.” Private equity firms control an estimated 8,000+ businesses in the U.S. and are responsible for 5% of the GDP (approximately US$600 billion in wages and benefits) and a significant share of the workforce (26 million American jobs, when including indirect jobs). As we enter what may be a prolonged downturn, private equity firms stand poised to use their dry powder (potentially combined with cheap debt due to low interest rates) to acquire distressed assets. The prospect of opaque investment firms with significant power and questionable ESG track records owning more and more of our economy may sound ominous. On the other hand, private equity firms, many of whom have large equity stakes and representation on company boards, wield much more influence on their portfolio companies than other types of investors employing a public equity or fixed income strategy. As such, private equity firms are among those best positioned in the asset management industry to enact positive systemic change.

**Q** WHY THE FOCUS ON THREE DIFFERENT CRISES?

**A** We want to be able to show clear trends in terms of how private equity firms respond to different crises. A private equity firm may be very vocal on one of these crises, but silent on the other two, even though all three are interconnected. The research is intended to show whether private equity firms are comprehensively taking systematic risks seriously and committing themselves to change.

**Q** HOW WERE THE SIX CHANGE CATEGORIES CHOSEN?

**A** We considered as many as a dozen different categories, as we designed the research methodology to encompass a wide range of potential actions that a private equity firm could take in response to a crisis. However, we decided to condense to just six change categories – three categories representing internal change and three categories representing external change – based on what we found in the first round of research results, which suggested some categories could be grouped together, and others could be removed from the research.

**Q** HOW DO YOU KNOW IF A PRIVATE EQUITY FIRM WILL FOLLOW THROUGH ON A STATED COMMITMENT OR CHANGE?

**A** To maintain the manageability of this study, this methodology assumes that once something is on the public record, a private equity firm is committed to taking that particular action. Of course, in “real-life,” it is critical that private equity firms accompany their public statements with appropriate policies, procedures, communications and training, and transparency and accountability mechanisms. This is discussed in further detail in the ‘Recommendations’ section of this report. Ultimately, we need better mechanisms for holding private equity firms accountable to these stated promises. However, given the lack of transparency in the sector, the findings of this study are limited in that regard.

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Mapping Interconnected Systemic Risks

No crisis occurs in a vacuum – most crises are the result of a set of interconnected risks and trends snowballing to create notable negative impacts. Rather than responding to negative impacts once they have manifested, we need to learn to respond to and address the root causes before they have an opportunity to snowball.

Consider the interconnected nature of the three crises discussed in this report – climate change, COVID-19, and racial injustice – each of which can be traced back to a set of other risks (see Fig. 2, above). At the center of the problem is the ‘financial profit maximization’ that is ingrained into the private equity industry and in most other parts of finance. Sometimes referred to more...
commonly as shareholder primacy or an interpretation (some, including ourselves, would argue misinterpretation) of fiduciary duty, this one factor has led to countless other systemic risks, highlighted in this report by the issues of financial engineering, natural resource exploitation, and human exploitation.\textsuperscript{13}

The irony is that each of these second-degree systematic risks negatively impacts the ability of investors to maximize their profits in the long-run. The end result, therefore, is a vicious cycle that would lock in future systemic shocks if not for immediate and all-encompassing systems change across both the private equity industry and capital markets in general.

It is worth noting that private equity firms often feel significant pressure to maximize financial returns due to the structure of their relationships with their investors, or limited partners (LPs). The private equity industry is highly dependent on institutional investors for capital, many of whom are re-evaluating their own understanding of their fiduciary duties. For instance, pension funds and sovereign wealth funds (SWFs), which are common types of investors into private equity funds, may recognize that a clean environment and worker protections may be highly valued by their beneficiaries (retirees or citizens), and that such beneficiaries may prioritize financial returns that do not come at the expense of a clean environment and worker protections. They may also recognize that in the long-run, climate change, inequality, and weak capital structures can destabilize their portfolios and therefore represent systematic risks which can negatively impact financial returns. In this sense, private equity firms should not just consider reporting to LPs on what is financially material to each portfolio company, but activities that are material to the health of the overall financial system and investors’ portfolios – in other words, systematic risks.\textsuperscript{14}

LPs have an important role to play in addressing these risks by using their voices and capital to shape incentives and mandates for how private equity firms make investment decisions and manage portfolios. For example, institutional investors could demand more reporting on


these and other sustainability risks, advocate for improved investment structures, negotiate limitations on certain practices with negative impacts, and take more chances on emerging managers which can allow new approaches to gain acceptance. We recognize that these issues are complex, and particularly in a period of low interest rates, institutional investors particularly value their private equity relationships and strategies that will help them meet their required rates of return (e.g., returns sufficient for pension funds to pay their pensioner liabilities). As such, these topics will be the dedicated subject of an upcoming research report and project from the Predistribution Initiative.
When it comes to a commitment to systemic change, private equity firms fall consistently short. Out of the 100 firms evaluated across three crises, we recorded a total of 84 public statements (an average of 28 statements per crisis) and 45 donations (an average of 15 donations per crisis). This is disappointing to say the least. As we’ve learned from every social change movement, being silent on an issue is akin to being complicit in the problem. Many private equity firms seem to struggle with even the most basic elements of being a responsible corporate citizen by failing to use their voice and wealth to acknowledge the pain of stakeholders and help support those in need.

Moreover, for an industry with notably high executive compensation, this trifecta of crises that disproportionately impacts marginalized communities and BIPOC would be an opportune time to recognize the systematic risks of inequality and “give back” to level the playing field for those who have been disadvantaged from our legacy broken systems. Prior to the COVID-19 crisis, 40% of Americans couldn’t afford a $400 emergency expense.15 Meanwhile, as the crisis has progressed and asset prices have increased (largely due to monetary policy interventions that disproportionately benefit investors), the wealth gap is only growing. Private equity firms could use some of their own wealth to support stakeholders who may be struggling to afford basic needs such as food, shelter, or healthcare.

Yet when it comes to changing the system that got us here, private equity firms are even more

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hesitant. In total, we evaluated 1,800 potential systemic changes (100 firms x 3 crises x 6 change categories) that a firm could have made, which were roughly evenly split between ‘internal changes’ and ‘external changes’. Of the 1,800 potential changes, we identified only about 135 internal or external changes for an uninspiring 7.5%. Given that many of these changes typically require the input and involvement of external advisors and investors, such changes may take longer to make and announce.

Put together, we identified 264 responses out of 2,400 potential responses (11%). More than a third of private equity firms (38%) took no action of any kind.

We also looked at the breakdown in quartiles. Of the 264 responses, the 25 most active firms (in terms of fundraising volume) contributed 125 responses versus 139 responses from the 75 other firms. Of the 135 internal or external changes, the same 25 firms announced 64 changes versus 71 changes from the remaining 75 firms.

The largest private equity firms of course have significantly more resources that can be used to take concrete actions in response to systemic and systematic risks. Therefore, it is not surprising that the top quartile of our research sample made notably more responses and changes than the bottom three quartiles on a percentage basis. However, even this response rate still falls far short of what is required to achieve true systems change.

These findings may not be surprising, but they are still troubling. Private equity firms wield a tremendous amount of influence in financial markets and in public policy. As more private equity firms tout their ESG and impact credentials, and given private equity firms’ position of strength to invest in companies troubled by the COVID-19 crisis, it is important that the industry be held to a higher standard of behavior.\(^\text{17}\)

While even this tepid level of response is unusual for the private equity industry, which traditionally has been opaque about its practices beyond announcing fund closings and portfolio transactions, there is still a long way to go. The fact that private equity firms are likely the most vocal they’ve ever been on social issues in 2020 is no coincidence. On the one hand, private equity firms increasingly recognize that many systematic risks like climate change are indeed material risks and should be taken into account when making investment decisions. But at the same time, private equity firms are finding themselves in the public spotlight more than ever as they encroach on more sectors of the economy and continue to raise institutional capital. The best way to address both trends is through increased transparency and accountability.

The days of private equity professionals operating with minimal transparency are over. For private equity firms to retain their social license to operate, it is imperative that they communicate publicly about how they are addressing these systemic crises and doing their part to advocate for and help achieve social, environmental, and economic systems change.

DATA

The following pages include additional data and analysis from the research. These charts and data points are intended to provide a snapshot of how private equity firms are responding to global crises and systematic risks. For any questions about the data or requests to see additional data, please contact the lead author at info@17c.org.

SAMPLE SIZE

Among the 100 firms in our research sample, 70% are based in the U.S., 21% are based in Western countries excluding the U.S. (United Kingdom, Canada, France, Switzerland, Sweden, Luxembourg) and 9% are based in Asia (Hong Kong, China, South Korea).
We evaluated 8 potential responses for each crisis – statement, donation, internal change (3 types), and external change (3 types). In total, we recorded 264 responses out of a potential 2,400 actions across the three crises (11%).

The most common type of response was a statement (84 total), followed by an internal change (73), external change (62), and a donation (45). However, the frequency and types of responses varied greatly across the three crises. COVID-19 elicited by far the most responses overall (114), significantly outpacing both racial injustice (76) and climate change (74). COVID-19 is also unique in that it only attracted international media attention in the last few months, while both climate change and racial injustice have been recurring themes that seem to slip in and out of the public consciousness.
This conclusion is supported by the number of firms that only responded to one crisis (32%), which is double the amount of firms that responded to all three crises (16%) but still less than the number of firms that didn’t respond to any crises (38%). This suggests most private equity firms are not taking systemic or systematic risks seriously, and in many cases are doing the bare minimum to show that they “care” without undertaking the serious kind of change that would prevent a continuation of the crisis.
INTERNAL CHANGES

We recorded a total of 73 internal changes out of a potential 900 internal changes (8.11%), with most of these coming in the form of increased employee training or resources (36 changes) or increased public reporting disclosures (29 changes). Comparatively, there were far fewer examples of new hires or changes to procurement practices (8) specifically in response to a crisis.

One of the most common examples of an internal change was the commitment to ESG and climate reporting, with many firms publishing an updated report or policy, or introducing one for the first time. The increase in climate reporting among private equity firms is commendable and is a positive step towards accountability, but many of these reports lack specifics about what a private equity firm plans to do to minimize its environmental footprint, both as an organization and among its investees.

We also saw many private equity firms organize employee training or sharing sessions around the issue of systemic racism, with the intention of creating a safe space for employees to discuss difficult topics. However, while having open conversations about the problem is a good sign, these conversations are unlikely to have much of an impact in the absence of additional changes to hiring, procurement, reporting and investment practices, which represent a more tangible step towards solving the DEI problem in the private equity industry. This stresses the importance of taking a systemic approach rather than a piecemeal approach to addressing these crises.

![Breakdown of Internal Changes by Crisis]

- **Hiring & procurement practices**
- **Employee training & resources**
- **Public reporting & disclosures**

<table>
<thead>
<tr>
<th>Crisis</th>
<th>Total</th>
<th>Climate Change</th>
<th>COVID-19</th>
<th>Racial Injustice</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Hiring &amp; procurement practices</strong></td>
<td>8</td>
<td>2</td>
<td>1</td>
<td>5</td>
</tr>
<tr>
<td><strong>Employee training &amp; resources</strong></td>
<td>36</td>
<td>9</td>
<td>10</td>
<td>5</td>
</tr>
<tr>
<td><strong>Public reporting &amp; disclosures</strong></td>
<td>29</td>
<td>17</td>
<td>5</td>
<td>7</td>
</tr>
</tbody>
</table>
EXTERNAL CHANGES

External changes have a high probability of bringing about direct systemic change and systematic market improvements because private equity firms have a much greater degree of influence over businesses, workers, the economy, and the financial system through their investment and portfolio decisions than they do through decisions that mainly affect private equity professionals and other industry insiders (though arguably a firm’s composition and culture will impact how it manages a portfolio). We recorded only 62 external changes out of a potential of 900 external changes (6.89%). By far the most common external change was engaging with portfolio companies to aid in the response to a crisis, especially in the case of COVID-19.

However, the majority of private equity firms seem unwilling to take the extra step of changing their investment decisions or their investment structures to help bring a stakeholder-centric model to life. To be fair, such changes can be complicated and require complex structuring that can take time to develop, particularly in regards to existing portfolio companies. Nonetheless, these are the kinds of changes that are necessary to achieve true systems change and build an inclusive society.

Additional examples of potential changes are included in the ‘Recommendations’ section of this report on page 28.
In the introduction to this report we made a distinction between non-systemic responses (i.e., those responses that do not address the roots of crises, like statements or donations) and systemic responses (i.e., those responses that represent a potential systemic shift like internal or external changes in how business and investment decisions are made). This distinction is important because truly addressing both systemic and systematic risks requires a systemic response. Therefore, we evaluated how many private equity firms made a non-systemic response to one or more of the three crises (thus acknowledging the issue) and then followed that up with a systemic response (thus attempting to address the issue). In other words, we wanted to see how many private equity firms were walking the walk versus just talking the talk.

The results show that few private equity firms are implementing significant changes. Of the 114 total responses to COVID-19, just 30 private equity firms made both systemic and non-systemic responses (26.3%). The response rates (i.e., making both systemic and non-systemic responses) for racial injustice (20/76, or 26.3%) and climate change (16/74, or 21.6%) were almost equivalent. Given that only 62 of the firms in our research sample made any kind of response, it seems that there is substantial room for improvement to translate words into action.
If we dig a layer deeper and look at how many firms hit across all four potential response types—and therefore are taking tangible and actionable steps—the numbers drop significantly. Only a handful of firms made a statement AND a donation AND an internal change AND an external change in response to any of the crises, with COVID-19 generating thorough responses from nine firms compared to just three each for climate change and racial injustice. There was not a single firm that made all six potential changes (three internal, three external) in response to any one of the three crises, although there were a handful of firms that made three or four changes. This suggests that private equity firms still have a long way to go when it comes to addressing systemic and systematic risks at their roots.

**How many private equity firms made both types of non-systemic responses (e.g., statement and donation) and both types of systemic responses (e.g., internal change and external change)?**

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<th>Crisis</th>
<th>3</th>
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<tbody>
<tr>
<td>Climate Change</td>
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<td>Racial Injustice</td>
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We are in a new age of corporate and financial communications. What may have been considered an acceptable public response a year ago is now often being called out as some combination of greenwashing, impact-washing and/or virtue-signaling. The increased skepticism and criticism aimed at private equity firms is likely to continue until we have a better mechanism for holding such firms accountable to a consistent set of standards.

We believe a truly comprehensive approach to addressing systemic crises and systematic risks would require a more thorough mapping of the issues and solutions. While we made intentional efforts to highlight issues and potential solutions throughout this report, ultimately, addressing these crises will require collaboration and cooperation among a wide range of stakeholders, including private equity firms themselves, as well as their LPs, civil society, advisors, policy makers, regulators, companies and labor advocates, among others.

To start, we offer here an initial set of 11 specific and actionable recommendations for private equity firms that want to show they are taking these crises seriously.

1 **Demonstrate that you are supporting policies with effective implementation.** Developing a set of policies (e.g., DEI; climate; ESG; etc.) and communicating about them publicly is a step in the right direction. However, for these policies to be implemented effectively, private equity firms should also take care to make sure each policy is backed up by:

- a system for communicating the policy across the organization and providing appropriate training;
- procedures for implementation, tracking, and reporting on progress;
- a clear delineation of roles and responsibilities for different team members;
- specific targets with achievable timelines;
- a commitment to holding team members accountable for implementing policies by having compliance and progress integrated into performance reviews and incentive structures (see more in point #2 below); and,
- a grievance mechanism that is made available to all stakeholders – internal and external – with non retaliation and whistleblower protection that ensures responsiveness of the organization and reporting to the highest level (e.g., board of directors).

2 **Conduct third-party audits of practices.** Private equity firms should consider engaging outside consultants who are experts in issues like climate science, DEI, or labor rights to provide a third-party perspective on what firms are doing well and where there is still room for improvement. The results of these audits should also be communicated to key stakeholders to ensure a degree of accountability, as well as follow-through on specific recommendations.

3 **Align financial incentives and valuation methodologies with ESG goals and systemic / systematic risk management.** Private equity firms have made progress on adding ESG staff to their teams, but these staff may have different performance targets and priorities from the investment teams, which in some cases may be in direct conflict. Private equity firms should reevaluate their compensation schemes to make sure individuals throughout the “capital markets value chain” – including workers, middle management, and senior management at portfolio companies, as well as individuals working within the asset manager – are properly incentivized to manage longer-term risks and maximize, to the extent practical, positive social and environmental impacts. As an example, a firm may reconsider the emphasis on the internal rate of return (IRR) metric and other time-value-of-money concepts that encourage on-the-ground and investment teams to strive to make as much money back as fast as possible, which can be in conflict with longer-term outlooks and risk management. Moreover, performance evaluations should not just be tied to near-term financial performance, like earnings growth or profit-and-loss budgets, but also longer-term measures of success that also consider systemic and systematic risks. Ultimately, such risks can manifest over longer periods of time, and it is not in the best interests of private equity funds’ investors to focus on near-term returns that result in future systematic problems.
4  **Fostering a culture of openness and intellectual curiosity.** The interventions mentioned in recommendation #3 above are often supported by a culture of transparency and open communication within an organization. The founders, partners, and C-suite leaders of private equity firms need to set the tone from the top, encouraging a culture of valuing the natural and human systems that underlie the economy and financial markets. Employees and other stakeholders should be invited to challenge the company to improve, and failures and opportunities to improve should be evaluated thoughtfully, versus punished reactively. This will help create a corporate environment where difficult questions and topics are regularly brought to the forefront rather than buried, and new ideas and solutions are diligently tested rather than ignored. This type of corporate culture can also foster an environment where risk and opportunity are better understood.

5  **Intentionally integrate principles of DEI into the firm and investment strategy.** Private equity firms should set and articulate relevant hiring, procurement, management, and investment targets with supporting strategies that encourage effective implementation. Practices should be in place not only at the firm and fund levels, but also at portfolio companies. Examples of practices that can lead to meaningful change include:

- conducting an audit of the firm’s existing practices and composition to identify weaknesses and to inform goals for improvement;
- hiring from a more diverse set of schools or organizations;
- partnering with non-profits who can help source diverse candidates and suppliers;
- implementing transparent hiring / promotion / pay practices with clear methodologies that result in pay equity;
- ensuring diverse leadership of the firm (e.g., C-suite, Board, Partners, Investment Committee) and responsible investment initiatives (e.g., those responsible for designing ESG and DEI initiatives);
- offering benefits that can support families and personal time (e.g. paid family leave for all genders);
- incorporating capacity-building and support programs with a particular emphasis on supporting typically marginalized populations;
- DEI training for all staff;
- reconsidering policies on when a background check is necessary and what types of criminal records are disqualifying;
- ensuring appropriate grievance mechanisms are in place and that existing policies and procedures do not inhibit their effectiveness (e.g., forced arbitration and certain aspects of non-disclosure agreements);
- seeking out investment opportunities with under-represented founders and in companies led by typically marginalized populations, including those that develop solutions in marginalized communities (e.g., addressing food or banking deserts, or promoting inclusive real estate development);
- developing transition strategies away from industries that contribute to human rights abuses (e.g., private prisons, detention centers, security firms, and companies that depend on their existence);
Adopt principles of ‘predistribution’ to share value with workers and communities. Predistribution is the concept of compensating stakeholders for the value that they create and the risk that they take in the value creation process in the first place, so that they don’t have to be as dependent on redistribution (where economic gains are redistributed via tax policy and charity) and so they can build resiliency. We believe that predistribution and redistribution are not mutually exclusive and that each would be most successful when applied in combination. But in our current system, workers are often treated as an expense to be minimized in service of greater profitability for investors. As we have learned through the COVID-19 crisis, it isn’t just those who provide financial capital who take risks and create value, but also workers who provide human capital. Workers should be compensated proportionate to their contributions through access to quality jobs and opportunities to build wealth, just as financial professionals are compensated for their contributions.

Studies have also shown that paying workers more and treating them better can result in stronger company performance, as workers are better incentivized to perform and given opportunities to build resiliency into their lives. In private equity, investors are often concerned with how investment teams are incentivized to create value, but arguably, workers in portfolio companies should also be considered as part of this motivational theory.

PRINCIPLES OF PREDISTRIBUTION CAN ALSO BE APPLIED TO COMMUNITIES AND THE ENVIRONMENT

While the argument for predistribution is relatively straightforward for workers, one could argue that it is also relevant for real asset investing, where infrastructure, real estate, or other projects are developed in communities, meaning the communities also take significant risk. As such, they should also be compensated via potential strategies including profit sharing, ownership stakes, governance roles, or other forms of community benefits agreements.

The environment (i.e., natural resource exploitation) is often also put at risk and used to create value. Can resource use be moderated under the assumption that water, air, and other natural resources are shared commons that are not actually free? Ultimately, what predistribution calls for is that the inputs to production are more thoughtfully and adequately priced and valued.

Private equity firms might consider profit-sharing programs or equity ownership for workers, in addition to providing a living wage, quality benefits (e.g. healthcare, paid sick leave, and other paid time off), and standard protections (e.g. freedom of association and collective bargaining, grievance mechanisms with no retaliation, proper protective equipment for working in dangerous conditions and during COVID-19). For contracted labor, it is important for private equity firms to at least adopt responsible contractor policies (RCPs). If these basic worker rights were in place via a predistribution lens, then there would less of a need for redistribution from private equity firms in the form of philanthropic initiatives and donations because workers would be able to build their own wealth and wouldn’t be as dependent on aid.

We encourage investors and other stakeholders to consider their existing practices and how they might reform them to address inequality. The Predistribution Initiative also invites investors to share reflections and lessons learned as contributions to the development of a Taskforce on Inequality-related Financial Disclosures (TIFD), which is being developed as a multi-stakeholder effort to address the systemic and systematic risks of inequality at their roots.21

7 Integrate climate considerations into every level of the organization. The increased severity and frequency of climate events (e.g., wildfires, hurricanes, flooding, extreme heat, extreme drought, etc.) demands a holistic response to begin to address the climate emergency. At the portfolio level, private equity firms should set science-based targets for their portfolio companies using commonly accepted frameworks where possible.22

At the fund manager level, firms should report climate risks according to the TCFD, transition their portfolio companies from carbon-intensive or non-renewable business models to more regenerative and renewable approaches, and shift future investment mandates away from the fossil fuel industry and towards opportunities in the circular economy. Private equity firms can also take actions to minimize their own carbon footprint by, for example, limiting air travel, restricting the use of single-use plastics, offering more vegan and vegetarian meal options, and

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21 For more information about the Taskforce on Inequality-related Financial Disclosures (TIFD) and to get involved, please visit www.thetifd.org
22 For more information about science-based targets, please visit https://sciencebasedtargets.org
COVID-19 SNAPSHOT

REDISTRIBUTION AS AN INTERIM TOOL TO LIMIT AN UNRAVELING FINANCIAL CRISIS, AND PREDISTRIBUTION AS A LONG-TERM, CONSISTENT TOOL TO PREVENT REOCCURRENCE OF INEQUALITY AS A SYSTEMIC (AND SYSTEMATIC) RISK

At this time of crisis, millions of people are struggling to pay their bills, keep food on their tables, and a roof over their heads. Given the significant wealth that has pooled to the larger private equity firms over the years, often with the support of preferential tax treatment, many of these firms—particularly the mega-fund managers—are well-positioned to be able to afford financial relief for their stakeholders who may be struggling. Depending on the size of the private equity firm, it could consider such contributions from its own compensation (i.e., management fees).

In terms of specific examples, for private equity firms with investments in sectors like housing or financial services, relief could come in the form of renegotiating customers’ commitments. Other private equity firms could look for ways to guarantee sick leave for portfolio company workers and/or reimburse healthcare costs. While these interventions may seem altruistic, they also support financial market stability and reduce risk for all stakeholders by reducing economic inequality.

Some private equity firms have already announced initiatives to provide relief funding to their portfolio companies, sometimes funded in part by executive pay cuts. This is laudable. It is important that such interventions are complemented by transparency as to how these funds are being allocated. What are the uses of these funds? Who specifically are they benefiting? And, of course, private equity firms should self-evaluate for consistency. Some of these same private equity firms have also retaliated against workers in their portfolio companies for their grievances about unsafe working conditions, raising very reasonable questions about the overall intentions of the firm and commitment to stakeholders.

The above suggested interventions can help temporarily offset some of the pain caused by a crisis like COVID-19, especially for individuals struggling to pay rent, mortgages, or other bills. But a longer-term solution would require a systemic approach that provides a strong social safety net and more opportunities for workers (and communities in the case of real assets) to share in economic gains, such as more equitable compensation models and responsible tax practices. This will help ensure that portfolio companies—and their stakeholders—have a better chance of remaining resilient in the face of mounting challenges.
sourcing energy from renewable sources. Thought should be given to the appropriate talent, experience, and skill sets needed to effectively manage climate risk. For instance, private equity firms should ensure the presence of climate risk expertise in their leadership committees, including the Investment Committee, as well as on portfolio company boards of directors, as appropriate.

Consider how your investment structures may be contributing to systemic and systematic risks. Many, though not all, private equity strategies rely on significant debt placed at the portfolio company level to generate returns (e.g., debt used for portfolio company acquisitions and/or dividend recapitalizations). Stakeholders such as workers and communities have become increasingly concerned about these practices, given their tendency to result in weak capital structures that can compromise quality jobs, benefits, the quality and affordability of goods and services provided, and the portfolio company’s continuation as a going concern. Indeed, non-financial corporate debt is at historical highs, leverage ratios are at their peaks, and covenants on debt had weakened substantially leading into the COVID crisis. There are also investor concerns about accounting practices, such as adjustments to reported earnings, that make leverage ratios look more attractive than they actually are. As the economy faces a new reality when most companies are private and cannot afford a downturn, these dynamics pose risks to all stakeholders — workers, communities, investors, and governments alike.

Governments are particularly in a difficult situation, as they have to decide how to most effectively use taxpayer contributions in a way that will benefit all. Private equity funds have benefitted from central banks’ interventions to lower interest rates, engage in quantitative easing, and even buy corporate debt. But many would argue that anyone benefitting from government support should be a good corporate citizen, and if private equity firms contributed to weak capital structures, then why should they be bailed out?

To be eligible for this support, and to avoid perpetuating systemic and systematic risks, private equity firms should commit to more responsible capital structures, have more transparency, and contribute their fair share of taxes. This includes adopting responsible tax practices not only at the portfolio company level, but also at the fund and fund manager levels.

It is critical that private equity firms start to disclose risks around these practices to their stakeholders, including investors. Without transparency, there is a lack of accountability and therefore a limited incentive to change current practices. Private equity investors might also look to the rise of benefit corporations and B Corps as one way to better integrate stakeholder and sustainability considerations across the organization.

9 Spend time with your stakeholders and build relationships with non-profits. Private equity firms may want to go beyond just writing checks to non-profits and instead focus on building long-term relationships with these organizations that includes a combination of financial support, volunteer time and two-way capacity building and learning. Many non-profits would benefit from a private equity professional’s expertise in activities like management and finance. Similarly, many private equity firms could benefit from learning from a non-profit’s perspectives and understanding of stakeholders and their concerns. Non-profits may also be well-positioned to facilitate a two-way dialogue between key stakeholders and private equity investors. These types of relationships can help build trust, empathy, and goodwill.
Private equity firms should not be afraid to engage with their stakeholders and take opportunities to self-evaluate their business practices and investment processes. Even the most diverse or mission-oriented companies may struggle to understand certain stakeholder groups or emerging concerns. It is critical that private equity firms approach systemic risks like climate change and economic inequality with an open mind, a willingness to learn and the flexibility to try different approaches.

Additionally, private equity firms may consider joining investor communities of practice focused on DEI and racial justice, such as Racial Justice Investing (RJI), which recently published a statement on best practices that was endorsed by both 17 Communications and the Predistribution Initiative, as well as a website to help share relevant resources and advance change.27

10 **Disclose all political spending and activities.** The private equity industry is increasingly in the public spotlight over its role in lobbying and political spend. Such spending may be, for instance, to advocate for taxing carried interest as capital gains, or even issues at the portfolio company level, like to protect surprise medical billing.28 While there is room for discussion about what the most effective policies would be, it’s impossible to engage in a vigorous debate without knowing exactly where each private equity firm stands on these issues. Private equity firms should publicly disclose political activity such as lobbying government officials, membership in industry associations, donating to candidates, supporting advocacy groups, etc. – on at minimum an annual basis. This disclosure should include activities at both the firm-level and the individual-level (at least for executives and other key individuals). The firm should also report on the political spend of its portfolio companies wherever feasible.

11 **Adopt public reporting using standardized disclosures.** Multi-stakeholder capitalism is of growing interest to business leaders around the world, but it is not possible without trust. Transparency and accountability are key in restoring public faith in the private equity industry and private sector. Private equity firms should be more transparent in how they are addressing these crises, with regular public reporting and disclosures. Where possible, private equity firms

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27 For more information about Racial Justice Investing (RJI), please visit: [https://www.racialjusticeinvesting.org](https://www.racialjusticeinvesting.org).
should use standardized disclosures such as those put forward by SASB, GRI, IMP, PRI, TCFD, and IRIS+ to report information in a consistent and easily comparable way (aligning with the SDGs where possible and practical). In terms of systemic and systematic risks, it is particularly important for private equity firms to consider frameworks being advanced by TCFD and the emerging TIFD, as certain risks may not seem material to a particular portfolio company, but are clearly material when added up across the economy and investors’ portfolios (e.g., living wage, quality of benefits etc.). Ensuring qualified individuals are responsible for each of these issues is a critical aspect of closing gaps.

This report makes it clear that private equity firms face an uphill climb when it comes to diligently responding to systemic and systematic risks and transforming their businesses for a sustainable future. However, to be fair, private equity firms are not alone in this climb, nor are they entirely responsible for their own journey.

The mechanics of investment management and finance are complex, which means that systematic risks require systemic solutions. We’ve laid out in this report and in the ‘Recommendations’ section what some of those solutions may be, both for private equity firms and which can be adapted for other types of asset managers.

However, it is also important to engage asset owners and allocators in the co-creation of solutions and consider their critical role. Institutional investors are increasingly cognizant of the threats that systemic risks like climate change, economic inequality, and racial justice pose to society and to their portfolios in the form of systematic risk. And these investors are taking strong steps in the right direction for issues that have gained in prominence and momentum among advocates. For instance, the Net-Zero Asset Owner Alliance is an international group of institutional investors with more than $5 trillion in combined assets who are committed to transitioning their investment portfolios to net-zero GHG emissions by 2050. And 450 institutional investors with over $40 trillion in assets are a part of Climate Action 100+, an initiative to engage the 100 largest corporate emitters to take significant action towards addressing the climate crisis.

To effectively address systemic and systematic risks, we cannot afford to be reactionary. Scientists are already warning of climate damage today that may be difficult if not impossible
to undo. While the racial justice movement has accelerated in recent months, millions of Black, Indigenous, and other People of Color around the world have been suffering for far too long or lost their lives due to inaction on issues of inequality. And as for COVID-19, thousands of workers continue to be forced to work in dangerous conditions because they cannot afford to say no, while taxpayers are left with the bill for risky capital structures designed to maximize near-term returns, often at the expense of quality jobs.32

To be proactive and take preventative measures against future crises, there are deeper problems to address with how investment decisions are actually made. For instance:

1. Returns and financial performance are often measured on a short-term basis or relative to short-term benchmarks; and,

2. Investors focus on risks that are financially material to a particular company, rather than risks that may accumulate across companies and impact their portfolios33

The end result is the destabilization of financial markets as systematic risks are either ignored or insufficiently addressed in a timely manner due to a lack of data and transparency and misaligned investment structures.

There are solutions in the works. Several organizations, researchers, and academics are exploring how to adjust time-horizons and methodologies against which investment performance is measured, as well as how to redefine the interpretation of materiality. For instance, Jon Lukomnik of Sinclair Capital and Jim Hawley of TruValue Labs are leading research that illuminates the importance of considering systemic and systematic risk in portfolio management.34 It will also be important for policy makers, regulators, and courts to reconsider the meaning of fiduciary duty and financial materiality in order to unlock the power of institutional investors and asset managers to address such risks.

But solutions require backing, both in terms of intellectual capital and financial capital. In this sense, we encourage all investors and private equity funds who recognize systematic risks to also contribute to field-building and policy efforts to help reinterpret fiduciary duty and financial materiality, particularly in the U.S. The PRI and other organizations focused on responsible investing are conducting leading research and advocacy on this front, to which investors could contribute. Private equity firms may also consider strategies to align their political spending to support such efforts.

Private equity firms have the potential to be the leaders in this global movement towards sustainable finance and a more responsible capitalism. A few kind words and well-intended donations are not going to move the needle. It’s time that private equity firms, together with their stakeholders, step up and do the work. The world is watching.

35 To learn more about the PRI’s work on fiduciary duty, please go to: https://www.unpri.org/policy/fiduciary-duty.