asset management group

April 28, 2017

The Honorable Steven Mnuchin
United States Treasury Secretary
U.S. Department of the Treasury
1500 Pennsylvania Avenue, N.W.
Washington, DC 20220

Re: Presidential Executive Order on Core Principles for Regulating the United States Financial System (February 3, 2017)

Dear Secretary Mnuchin:

The Asset Management Group ("**AMG**")[1] of the Securities Industry and Financial Markets Association ("**SIFMA**") appreciates the opportunity to provide input to the U.S. Department of the Treasury ("**Treasury**") as it develops its report (the "**Report**") in response to President Trump's Executive Order on Core Principles for Regulating the United States Financial System (the "**Executive Order**").[2]

We support the goals of the Executive Order, and agree that adherence to the principles outlined in the Executive Order (the "**Core Principles**") would better ensure sound regulatory oversight of the U.S. financial markets. In providing our views of regulations in light of the Core Principles, AMG hopes to assist the Treasury Department in refining financial regulations to ensure that they are effective, efficient and appropriately tailored, which in turn will promote vibrant U.S. capital markets, to the benefit of American investors.

AMG's comments focus on the following regulatory issues that are particularly important to our members and that we believe need recalibration in accordance with the Core Principles: (1) repealing attempts to apply macroprudential regulation to non-banks, including inappropriate non-bank systemic risk designations, and revisiting bank capital and other prudential policies that are unduly harming capital markets and investors; (2) recalibrating certain recent domestic regulations proposed or finalized by U.S. regulators, including the Securities and Exchange Commission ("**SEC**" or "**Commission**") and the Commodity Futures Trading Commission ("**CFTC**") that may harm investors and the markets; (3) changing the U.S. Department of Labor's ("**DOL**") fiduciary

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[1] SIFMA AMG brings the asset management community together to provide views on policy matters and to create industry best practices. SIFMA AMG's members represent U.S. and multinational asset management firms whose combined global assets under management exceed $39 trillion. The clients of SIFMA AMG member firms include, among others, tens of millions of individual investors, registered investment companies, endowments, public and private pension funds, UCITS and private funds such as hedge funds and private equity funds.

[2] Please see appendix for the glossary of defined terms.

rule into a uniform standard that will apply to all retail investors receiving personalized investment advice without unduly adding costs and burden; (4) addressing unintended consequences for so-called "covered funds" under the Volcker Rule; (5) reconsidering the current SEC process for approving exchange-traded funds ("**ETFs**"); and (6) leading ongoing international regulatory efforts that will disproportionately affect U.S. markets and U.S.-based asset managers, insurers, and their clients.

Our key recommendations are as follows:

Topics and Recommendations for Treasury to Include in the Report	**Necessary Action**
A. Macroprudential Regulation of Non-Banks and Capital Markets	
1. FSOC and Non-Bank Systemic Risk Designations	
Congress should repeal the authority of the FSOC to designate non-bank financial companies as systemically important financial institutions ("**SIFIs**").	Congressional Action
Treasury should officially recognize the benefits of asset management and market-based finance in the Report, and endorse a repeal of the non-bank SIFI designation authority under Title I of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("**Dodd-Frank**").	Treasury Action
Pending Congressional action and in accordance with President Trump's April 21, 2017 memo, the Financial Stability Oversight Council ("**FSOC**") should not vote for any non-emergency designation, reevaluate whether designations for non-bank entities are appropriate, reform its processes to ensure due process, improve its transparency, and fix other flaws outlined by the AMG and other industry groups.	FSOC Action
The FSOC should issue a letter or formal statement acknowledging that its review of asset managers, as well as asset management products and activities, has identified no systemic risk and explicitly rejecting the macroprudential approach to regulation of this sector.	FSOC Action
The FSOC should pivot to focusing on its responsibilities as an inter-agency forum, monitoring market developments and facilitating information-sharing and regulatory coordination.	FSOC Action

2. Prudential Requirements Affecting the Capital Markets and Qualified Financial Contracts	
The Federal Deposit Insurance Corporation ("**FDIC**"), Federal Reserve Board of Governors ("**Federal Reserve**"), and Office of the Comptroller of the Currency (**"OCC**") (collectively the "**federal banking agencies**") should revise the Supplementary Leverage Ratio ("**SLR**") to recognize the exposure-reducing effect of customer initial margin provided to the banking organization in client cleared derivative transactions and held separately from bank proprietary assets.	Federal Banking Agencies – Joint Rulemaking
The federal banking agencies should withdraw the net stable funding ratio ("**NSFR**") proposal given that NSFR layered on top of other bank capital requirements will produce little benefit and impose material costs on derivative, repo and securities financing transactions. If the federal banking agencies decide to finalize the proposal, they should significantly improve the standard to avoid undue burden and negative impacts to the derivatives, repo and securities financing transactions.	Federal Banking Agencies – Joint Rulemaking
The Federal Reserve should revise its Single-Counterparty Credit Limits ("**SCCL**") rule proposal to take a more targeted approach to addressing regulatory concerns.	Federal Reserve Rulemaking
The federal banking agencies should not finalize the proposed rules restricting default rights provided in Qualified Financial Contracts ("**QFCs**"). Congress, rather than the federal banking agencies, should take steps to secure cross-border recognition of Title II of the Dodd-Frank Act. To ensure the enforceability of QFCs governed by non-U.S. law entered into by a covered entity, Congress should work with other countries to achieve mutual recognition of all special resolution regimes, including Title II of the Dodd-Frank Act, irrespective of the QFC's governing law. Absent an agreement on mutual recognition, the U.S. should address the issue through statutory change, not prudential regulation. Any steps taken to address cross-border recognition of Title II of the Dodd-Frank Act should be narrowly tailored to achieve that result without impacting rights under domestic law and in ordinary bankruptcy.	Congressional Action or Federal Banking Agencies – Joint Rulemaking

B. SEC Regulation of Asset Management Products and Services	
1. Stress Testing	
Congress should repeal Section 165(i) of Dodd-Frank.	Congressional Action
The SEC should refrain from implementing any stress testing requirement on asset managers, funds, or the financial system until the requisite research is completed or Congress addresses the issue through legislation.	SEC Action
Treasury should also recommend that the United States work with the International Organization of Securities Commissions (“**IOSCO**”) to delay its work related to the Financial Stability Board’s (“**FSB**”) recommendations on stress testing until the United States determines whether to proceed on this issue.	Executive Order
2. Data Collection	
The SEC should propose amendments to the Data Modernization final regulations to reallocate the information to be reported between existing forms and the new reporting form in order to address public reporting disclosure concerns.	SEC Rulemaking
The SEC should also propose amendments to Form ADV to remove the new public reporting requirements related to separate account information, recognizing that the harms of public reporting outweigh any potential benefit.	SEC Rulemaking
The SEC and CFTC should issue proposed rules that seek to rationalize and adjust existing reports to ensure the reports meet the needs of regulators and are not duplicative in nature.	SEC and CFTC Rulemaking
The SEC should also immediately extend the compliance deadline by 18 months on both the changes to Form ADV and the new reporting requirements under the Data Modernization final regulations.	SEC Guidance or Rulemaking
3. Electronic Delivery of Regulatory Documents	
Treasury should recommend universal consent to all regulatory documents, rather than require consent on a per-agency, per document, per account basis.	Executive Order or Congressional Action
The SEC should finalize Rule 30e-3 as soon as the Commission has a new Chairman confirmed.	SEC Rulemaking

The SEC should work together with the DOL to consider additional rule changes that could be made to continue to lessen the administrative burden from regulatory consent documentation.	SEC and DOL Rulemaking
4. Liquidity Risk Management	
The SEC should immediately issue a delay for the final rulemaking for at least 18 months from the compliance deadline.	SEC Guidance
During the delay period, the SEC should consider the unintended consequences that defeat the intended "workability" of the rule, and issue a proposed rule that is principles-based in nature to address these issues.	SEC Rulemaking
5. Business Continuity Planning and Transaction Planning	
The SEC should abandon the proposed rule and issue guidance on business continuity planning that builds upon previous guidance under Rule 206(4)-7 under the Investment Advisers Act of 1940 ("**Advisors Act**").	SEC Guidance
Should the SEC determine that a new rule is necessary, it should be re-proposed, focusing solely on business continuity planning, removing the "fraudulent" liability for business continuity practices, and removing any requirements for "transition planning."	SEC Rulemaking
6. Leverage and the Use of Derivatives	
The SEC should withdraw its proposal and not set leverage limits unless future evaluation of the enhanced data received pursuant to the data reporting rule indicates clear justification for limits.	SEC Rulemaking
The SEC should codify and modernize the asset segregation requirements to correct a number of known issues outlined in AMG's comments to the SEC.	SEC Rulemaking
C. CFTC Regulation of Funds and Advisers	
The CFTC should return to its previous decision to avoid overlapping regulation of SEC-registered funds and advisers by reversing its 2012 amendments of CFTC Rule 4.5 and reverse its revocation of CFTC Rule 4.13(a)(4).	CFTC Rulemaking

The CFTC should revise its policy on "one swap" and inadvertent commodity pools in order to avoid unnecessary, extraterritorial and overlapping regulation of funds and advisers.	CFTC Guidance
If the CFTC does not zero out the registration overlap with the SEC, it should make further improvements to substituted compliance requirements for those dually-registered entities.	CFTC Rulemaking and/or Guidance
D. CFTC Regulation of Derivatives Markets	
1. Position Limits	
The CFTC should not impose further position limits without determining necessity to do so and, if necessity is determined, establish limits that take into account the specifics of each contract and market. The CFTC should also revise its aggregation standards to remove burdensome disaggregation notice filings, remove the unworkable "substantially identical trading strategies" aggregation standard, and allow independent account controller disaggregation to apply to exempt commodity trading advisers.	CFTC Rulemaking
2. Regulation Automated Trading	
The CFTC should not impose additional burdens upon designated contract markets through Regulation Automated Trading ("**Reg AT**") or, if it believes additional controls are necessary, should focus on non-redundant risk measures that apply on a market-wide basis.	CFTC Rulemaking
3. Central Execution of Swaps	
The CFTC should re-tool swap execution facility requirements to broaden permissible methods of execution to any method that provides sufficient transparency; improve the made-available-to-trade designation process to provide workable standards for determining the subset of cleared products that should also be mandated for central execution; address made-available-to trade issues related to package transactions such that only liquid, standardized packages capable of being traded on swap execution facilities are required for central execution; and maintain impartial access standards to ensure fair access to liquidity for all market participants. The designated contract markets—including, those within the Chicago Mercantile Exchange and Intercontinental Exchange—should revise their rulebooks to permit swaps traded on swap	CFTC Rulemaking and Designated Contract Market Rule Changes

execution facilities to be exchanged for futures via the exchange for related product procedures.	
E. DOL Fiduciary Rule	
The DOL should defer application of the DOL Fiduciary Rule until completion of the review directed by the President's February 3, 2017 Executive Order. The DOL should repeal the DOL Fiduciary Rule, after which the SEC or the Financial Industry Regulatory Authority ("**FINRA**") should propose a uniform best interest standard that applies to personalized investment advice for all retail investors.	SEC and DOL Rulemaking
F. Volcker Rule	
Congress should repeal the Volcker Rule. To the extent a full repeal is infeasible, Congress should consider replacing Volcker with tailored requirements, limiting the covered fund provisions to (1) funds that principally engage in proprietary trading; and (2) maintain the prohibition on bailing out sponsored covered funds.	Congressional Action
The regulatory agencies should narrow the definition of "covered funds" to exclude from the definition of covered funds vehicles that are not principally engaged in impermissible proprietary trading.	Congressional Action or Joint Regulatory Guidance
At a minimum, Congress should pass tailored legislative fixes that address the Volcker covered fund problems, such as H.R. 4096, which passed the House last year and would have addressed the naming prohibition issue (i.e. incorporate exceptions from Section 23 of Federal Reserve).	Congressional Action
The regulatory agencies should automatically grant the permitted two-year extension for seeding (beyond the initial one-year extension) for all bank investments in covered funds. They should also clarify that the use of bank assets to seed investment strategies for the purpose of demonstrating investment performance is not considered to be short-term trading for the purposes of the Volcker Rule's proprietary trading restrictions.	Joint Regulatory Guidance
The regulatory agencies should issue guidance that states that they will not enforce the naming restrictions, pending enactment of a legislative fix.	Joint Regulatory Guidance
In addition to correcting the definition of "covered fund," the regulatory agencies should amend the rule or issue guidance	Joint Regulatory Rulemaking or

establishing that credit exposures extended in the ordinary course of providing custody services are not prohibited by the Super 23A provisions.	Guidance
G. ETF Approval Process	
The SEC should issue a proposed rule that would fast track "plain vanilla" ETF approvals and authorize by individual application non-transparent actively-managed ETFs.	SEC Rulemaking
The SEC should issue guidance outlining one standard for exemptive relief that applies to all market participants.	SEC Guidance or Rulemaking
H. International Regulatory Efforts	
The United States should increase its participation in international bodies, and take a greater leadership role in international regulatory coordination related to the capital markets.	Congressional Action or Executive Order
The U.S. should consider whether the promulgation of international recommendations follows a sufficiently transparent process and whether, in some cases, the international efforts undermine U.S. administrative standards and cost-benefit analysis that must be met for U.S. regulations. While international coordination is important, it should not supplant the role and processes of U.S. regulators domestically. As such, the U.S. should reject implementing international standards under such circumstances.	Congressional Action or Executive Order
To the extent that an international standard, recommendation, or principle currently under consideration by an international body or not yet addressed in jurisdictions domestically does not align with the Core Principles, the United States should advocate forcefully for the international regulatory body to either withdraw or amend it to address the United States' concern.	Congressional Action or Executive Order
The United States should also ask international bodies to stay their regulatory efforts until key leadership of U.S. regulatory agencies are in place to engage international bodies and prioritize America's best interests.	Executive Order

I. Background

A. President Trump's Executive Order

On February 3, 2017, President Trump issued Executive Order 13772, which outlined the following Core Principles for regulating the U.S. financial system: (a) Empower Americans to make independent financial decisions and informed choices in the marketplace, save for retirement, and build individual wealth; (b) Prevent taxpayer-funded bailouts; (c) Foster economic growth and vibrant financial markets through more rigorous regulatory impact analysis that addresses systemic risk and market failures, such as moral hazard and information asymmetry; (d) Enable American companies to be competitive with foreign firms in domestic and foreign markets; (e) Advance American interests in international financial regulatory negotiations and meetings; (f) Make regulation efficient, effective, and appropriately tailored; and (g) Restore public accountability within Federal financial regulatory agencies and rationalize the Federal financial regulatory framework.[3]

It also directed the Secretary of the Treasury to consult with the heads of the member agencies of the FSOC and report to the President within 120 days (and periodically thereafter) on the extent to which existing laws, treaties, regulations, guidance, reporting and recordkeeping requirements, and other Government policies promote the Core Principles. The Report should also identify any laws, treaties, regulations, guidance, reporting and recordkeeping requirements, and other Government policies that inhibit Federal regulation of the United States financial system in a manner consistent with the Core Principles.[4]

The Recommendations to Treasury in this letter seek to advance the Core Principles. U.S. asset management and capital markets are the largest and most developed in the world. The capital markets empower Americans to achieve their financial goals by helping them save for retirement and other lifetime priorities and they promote economic growth and enhance the competitiveness of American companies by providing additional sources of capital. In essence, capital markets are a better way to finance corporate America. Corporations can be less dependent on bank funding, which could reduce system-wide risk in the system. Rebalancing financial regulatory requirements for this industry to reduce complexity, costs, and duplicative regulatory requirements will create a better, more rational financial regulatory framework where rules are tailored and appropriate to address sound policy goals. While the list of potential issues that could be addressed is rather long, we have focused in this letter on some of the larger, more pressing concerns for asset managers and their clients, which we believe will have the most impact on advancing the Core Principles.

B. Overview of the Asset Management Industry

The U.S. asset management industry is made up of a large number of diverse firms and individuals that provide investment advice (whether on a discretionary or non-discretionary basis) to clients. As of 2017, nearly 34,500 SEC and state-registered investment advisers served to help individuals and institutions allocate $67.1 trillion of investments across a wide range of asset classes,

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[3] Exec. Order No. 13,772, 82 Fed. Reg. 9965 (Feb. 3, 2017).

[4] *Id.*

including early stage equity investments in venture capital backed companies, publicly traded equity and debt of larger companies, and local, state, and federal bonds.[5]

Asset managers and their products and services are highly regulated and subject to extensive public disclosure requirements imposed by the entire complex of federal securities laws: the Securities Act of 1933, the Securities Exchange Act of 1934, the Commodity Exchange Act, the Advisers Act, and the Investment Company Act of 1940 ("**40 Act**"). The last two are specifically dedicated to ensuring disclosure to both the SEC and investors that is tailored to funds and advisers, including, for example, information about investment strategy, related risks, valuation of portfolio securities, conflicts of interest, and, in the case of funds, Board governance. Importantly, registered funds are subject to comprehensive substantive regulation under the 1940 Act, including regulation of fund structure, governance, advisory contracts, conflicts of interest, and leverage, to name a few. These regulations were developed in the years after the Great Depression, and created a robust framework that has stood the test of time and promoted the growth of the largest retail asset management market in the world.

U.S.-registered investment companies (e.g., mutual funds and ETFs), other types of investment vehicles, and separate accounts that asset managers serve are investors in the capital markets, lenders to issuers, and large holders of U.S. commercial paper. They also are important contributors to augment liquidity in the capital markets. Products like mutual funds empower retail investors to access these investments and save for their long-term goals. Without these vehicles, U.S. capital markets would be far less able to provide the benefits they do today, such as helping retail investors save for retirement, pay for college, start a small business, or pay for a home of their own. Mutual fund investments also provide the capital the capital markets need to power the American economy, complimenting bank credit and reducing reliance on the federal safety net. These benefits, in turn, reduce systemic risk and promote economic growth. Professional investment expertise and risk management provided by asset managers benefits retail and institutional investors alike, while promoting efficient capital allocation and financial stability.[6]

Asset managers operate in a highly competitive marketplace, which has driven down management fees consistently over time, and resulted in innovative new products, such as ETFs, providing increasingly cost-effective financing for businesses and governments. Poorly designed regulation distorts the market and impairs those benefits. Excessive regulation impacts small and mid-sized firms most acutely, as well as small and potentially underserved investors. The current regulatory regime has resulted in significant consolidation within asset management and a higher bar

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[5] SIFMA, US Quarterly Highlights, First Quarter 2017 (Apr. 18, 2017), http://www.sifma.org/research/item.aspx?id=8589965772.

[6] *See, e.g.*, Jonathan Hill, Member, European Comm'n, Speech at the Finance Watch Conference: Finance at Your Service – Capital Markets Union as an Instrument of Sustainable Growth (Feb. 4, 2015), http://europa.eu/rapid/press-release_SPEECH-15-4144_en.htm ("[W]e need both financial stability and growth: we need sustainable growth. That is the new Commission's number one priority;" and "Well-functioning capital markets also help encourage greater diversity in funding, which reduces concentration of risk so they not only free up capital for growth but also support and strengthen financial stability. After all, it's important to remember that 'capital markets' are not some abstract construct – they are someone's pension savings, someone's 'rainy day' money which is channeled to growth.").

to entry, basically setting a trend for the industry to become even more consolidated in the future.[7] We urge all of the U.S. financial regulators, and in particular the primary regulators for different segments of the markets, to follow the Core Principles as a means of reversing the consolidation trend and seeking to ensure that the regulatory problems already manifesting within the banking sector are not repeated in the asset management sector.

It is important to note – especially as bank regulators globally often seem to fail to understand – that asset managers are very different from banks.[8] Asset managers act on behalf of their clients, not on behalf of themselves. As such, asset managers generally do not use their own assets to fund their client relationships. As fiduciaries, asset managers provide access to, diversifying and reducing risk for issuers and fund investors, and actively manage risks associated with, the particular investment mandates of their clients. Therefore, from an overall systemic risk perspective, they function as risk reducers rather than risk creators. In this capacity, the basic characteristics of the relationship between an asset manager and its clients are uniform, highly substitutable, and promote financial stability: asset managers provide advice to, and act as agents on behalf of, clients and fund investors seeking exposure to certain investment strategies and their attendant investment results. Moreover, asset managers invest their clients' assets pursuant to investment mandates determined by their clients. Managers apply their professional judgment and considerable resources to help their clients achieve their investment, retirement and other lifetime financial goals.

Although investors hire an asset manager to help them take market risk, existing regulations applicable to asset managers and their regulated products mitigate operational risks. An asset manager is not permitted to commingle client assets with its own assets, and client assets typically are maintained with a separate custodian. Additionally, a manager's creditors do not have recourse to the assets of the manager's clients. Reciprocally, a manager's clients do not have recourse to the manager's assets or to the assets in other funds or clients managed by the asset manager.

Asset managers disclose investment risks, do not guarantee positive investment results, and do not back-stop investment losses.[9] This is an important feature of the relationship between an

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[7] Investment Company Institute, 2016 Investment Company Fact Book, https://www.ici.org/pdf/2016_factbook.pdf (last visited Apr. 25, 2017); *see also* Bill McIntosh, *Fund Consolidation: Man Group strikes deal to acquire FRM*, The Hedge Fund Journal (June 14, 2012), http://www.thehedgefundjournal.com/content/fund-consolidation.

[8] Financial Stability Board, *Policy Recommendations to Address Structural Vulnerabilities from Asset Management Activities* (Jan. 12, 2017), http://www.fsb.org/wp-content/uploads/FSB-Policy-Recommendations-on-Asset-Management-Structural-Vulnerabilities.pdf. ("[F]rom a purely systemic perspective, funds contain a specific 'shock absorber' feature that differentiates them from banks."); *see also* Nellie Liang, Dir., Program Direction Sec. of the Off. of Fin. Stability Pol'y & Res., Bd. of Governors of the Fed. Res. Sys., Remarks at the Brookings Institution Asset Management, Financial Stability and Economic Growth Conference (Jan. 9, 2015), http://www.brookings.edu/events/2015/01/09-asset-management-financial-stability-economicgrowth ("Mutual funds in their current form have been around for a long time . . . without noticeably contributing to systemic risk.").

[9] We acknowledge that in the past certain money market fund sponsors have chosen to support their funds' net asset values. Those instances are the exception to the rule. Further, even in those cases, sponsors were not required to do so.

asset manager and its clients, and is well understood by fund investors and clients. Under the Advisers Act, asset managers are required to disclose to investors the risk of the particular investment strategies in which the investors' assets are being invested. Such risk disclosures typically include language that the investors may lose some or all of the value of their investments and that investment results are not guaranteed. Many asset managers are also global in nature, subject to regulations in multiple jurisdictions (that are not always harmonized with one another).

C. Post Crisis Regulation of Asset Management

Yet, despite the many safeguards inherent in the asset management industry's structure, since the financial crisis the industry has been subjected to an avalanche of regulations, many of which are a carryover of banking or public company regulations, that are directly harming investors and the broader capital markets. Much of the new regulations on the asset management industry stemmed from the government bailout of certain other financial entities, which prompted Dodd-Frank. Though asset managers did not cause the financial crisis, they were too often collateral damage in Dodd-Frank and related post-crisis rulemaking, which significantly expanded the regulatory requirements on asset managers, the products they offer, and the instruments they invest in on behalf of their clients, including registration and reporting requirements for almost all managers of private funds, separate accounts, and other investment assets.

The majority of the new regulations on asset managers have directly followed macroprudential regulatory pressure, or the attempts by central bankers and bank regulators to extend bank-style prudential regulation to non-banks and capital markets in order to expand their jurisdiction and to contain the effects of their unprecedented monetary policy actions. As prudential regulators have completed reforms for the banking sector, they have claimed that the risks addressed for banks will now migrate to non-banks, given the industry's "increasing significance to financial markets and the broader economy."[10] These beliefs are not supported by any empirical facts or data concerning the asset management industry and should not form the basis for rulemaking. In essence, prudential regulators see all financial institutions as banks, and attempt to regulate all financial institutions like they are banks. This is inappropriate, and causes harm to investors and the capital markets.

Further, monetary policy that was designed to incent investors to reach for yield caused central bankers to worry about the consequences of their actions and to seek an unprecedented level of control over capital markets by substituting regulators' judgments for investors' judgments. Central bankers have long resisted that urge[11] and many still do.[12] Others failed to heed their

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[10] U.S. Financial Stability Oversight Council, *FSOC 2016 Annual Report*, https://www.treasury.gov/initiatives/fsoc/studies-reports/Documents/FSOC%202016%20Annual%20Report.pdf.

[11] *See* Ben S. Bernanke, Member, Bd. of Governors of the Fed. Res. Sys., Remarks before the New York Chapter of the National Association for Business Economics: Asset-Price "Bubbles" and Monetary Policy (Oct. 15, 2002), http://www.federalreserve.gov/Boarddocs/Speeches/2002/20021015/default.htm. (In that speech, Mr. Bernanke explained that it is not realistic to expect that the FRB can "estimate the unobservable fundamentals underlying equity valuations" better that the financial professionals whose collective information is reflected in asset-market prices. He also noted that mere changes in asset prices are not good

warnings and sought to expand prudential regulation beyond its appropriate scope.[13] Expanding macroprudential policies to asset managers conflicts with many of the Core Principles, because it runs contrary to empowering Americans to make independent financial decisions, inhibits economic growth and vibrant financial markets, and forces regulations on the asset management industry that are not efficient, effective, or appropriately tailored.

In its targeted focus for financial stability and search for systemic risk, in 2008 the FSOC turned its sights on asset management, first directing the Office of Financial Research ("**OFR**") to study asset management, presuming systemic risk. It continued with a search for hypothetical systemic risks related to asset management products and activities. International regulatory bodies including the FSB and IOSCO have also focused on asset management firms, products and activities, likely due, at least in part, to the influence of U.S. prudential regulators. Each oversight body began its review by focusing on entity designations, and subsequently pivoted to focusing on hypothetical systemic risks associated with certain asset management products and activities when failing to find systemic risk at the individual entity level.

Enhancing the already sound regulatory regime for asset management is an essential component to ensuring our capital markets remain strong. The U.S. capital markets are the envy of the world. They provide sources of funding for businesses, increase options for savers, and ultimately make the economy more resilient. The U.S. recovery from the financial crisis was

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indicators that the new asset price is irrational or unjustified, and stated: "[T]he Fed cannot reliably identify bubbles in asset prices. . . . [T]o declare that a bubble exists, the Fed must not only be able to accurately estimate the unobservable fundamentals underlying equity valuations, it must have confidence that it can do so better than the financial professionals whose collective information is reflected in asset-market prices. I do not think this expectation is realistic, even for the Federal Reserve.").

[12] *See, e.g.*, Jerome H. Powell, Member, Bd. Of Governors of the Fed. Res. Sys., Speech at the Stern School of Business, New York University (Feb. 18, 2015), http://www.federalreserve.gov/newsevents/speech/powell20150218a.htm ("[U]nless there is a *plausible* threat to the core of the system or potential for damaging fire sales, I would set a high bar for supervisory interventions to lean against the credit cycle. Such interventions would almost surely interfere with the traditional function of capital markets in allocating capital to productive uses and dispersing risk to the investors who willingly choose to bear it." (emphasis added)). That concept of probability has been notably absent from much of the unbridled speculation regarding systemic risk, but it should be an essential filter in the FSOC's inquiry. *See also* Esther L. George, President & CEO, Fed. Res. Bank of Kan. City, Speech at the Financial Stability Institute/Bank for International Settlements Asia Pacific High Level Meeting: Monetary and Macroprudential Policy: Complements, Not Substitutes (Feb. 10, 2015), http://www.kansascityfed.org/publicat/speeches/2015-George-Manila-BIS-02-10.pdf. ("[S]potting asset price bubbles or financial imbalances in real-time is notoriously difficult—something that is just as true today as in the past." and "It remains true that we can't identify bubbles in real time, or at least don't know the proper time and manner to intervene to stem their rise."); and ("I often hear the view that macroprudential policy should be the 'first line of defense' for maintaining financial stability. Unfortunately, this approach expects too much of tools for which our understanding is imperfect.").

[13] *See* Governor Daniel K. Tarullo, *Advancing Macroprudential Policy Objectives*, Speech at the Office of Financial Research and Financial Stability Oversight Council's 4th Annual Conference on Evaluating Macroprudential Tools: Complementarities and Conflicts (Jan. 30, 2015), https://www.federalreserve.gov/newsevents/speech/tarullo20150130a.htm.

relatively smooth precisely because of the participation of asset managers in our capital markets, which hedge risks.[14] Going forward, the future of this country is closely tied with the health of our markets. President Trump's ambitious plan to address U.S. infrastructure concerns, for example, relies on our capital markets, which fund companies and municipalities and the long-term projects that may be developed as public-private partnerships, expanding and creating jobs for many. Yet, in an effort to make our markets "safer," macroprudential-like regulations have been issued that have caused market distortions, undermining these benefits, and make the system riskier, rather than safer.

Many of the post-crisis asset management regulations are inefficient or ineffective, creating unnecessary and costly red tape that will take money out of the pockets of savers and investors. Ultimately, the regulations are directly harming – or have the potential to harm – investors and our capital markets at large, thwarting progress and growth and we urge Treasury to include the recommendations we make below in the Report.

II. Recommendations

A. Macroprudential Regulation of Asset Managers and Capital Markets

1. FSOC

Much of the recent regulatory activity in asset management was prompted by (or occurred against the backdrop of) misguided efforts of newly created or empowered bodies, such as the FSOC, FSB, and IOSCO, as well as research-oriented bodies such as the OFR and Bank for International Settlements ("**BIS**"), to identify and stamp out "systemic risk." Their efforts were fatally flawed from the start for several reasons: (1) there was no consensus definition of systemic risk;[15] (2) the tools and techniques necessary to identify it and design policies to address it still do not exist;[16] (3) regulatory bodies such as the FSOC were dominated by bank regulators with little or no

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[14] Sir Jon Cunliffe, Deputy Governor Fin. Stability, Bank of Eng., Speech at the City of London Corporation and Open Europe Conference: Financial Stability, the Single Market and Capital Markets Union (Jan. 20, 2015), http://www.bankofengland.co.uk/publications/Documents/speeches/2015/speech789.pdf. ("It is very probable that one of the reasons the US has recovered faster from its financial crisis than Europe is that in the US banks do not dominate the provision of finance to anything like the same degree as in the EU.").

[15] "The term 'systemic risk' has an interesting history. If you go back 10 years and do some Google searches for it, you won't find out that much. Post-financial crisis, it's become kind of the buzzword or grab bag, so to speak, that people use to rationalize a variety of interventions in financial markets." Douglas Clement, *Interview with Lars Peter Hansen*, The Region (Dec. 17, 2015), https://www.minneapolisfed.org/publications/the-region/interview-with-lars-peter-hansen.

[16] *See* Douglas Elliott, *Regulating Systemically Important Financial Institutions that are not Banks*, Brookings (May 9, 2013), https://www.brookings.edu/research/regulating-systemically-important-financial-institutions-that-are-not-banks/; Matthew Richardson, *Regulating Wall Street: CHOICE Act vs. Dodd-Frank, NYU Stern School of Business and the NYU School of Law* (Mar. 1, 2017), http://www.stern.nyu.edu/experience-stern/about/departments-centers-initiatives/centers-of-research/global-economy-business/development-initiatives/financial-regulation.

experience or expertise with non-banks and capital markets;[17] and (4) they were directed to use bank supervisory tools to regulate non-banks (or they naturally looked for the banking risks and turned to bank supervisory tools) because they were both familiar.

Unfortunately, their familiarity did not make them relevant to non-banking industries like asset management. In fact, they were wholly inapposite. These problems were compounded by unsound administrative practices that they attempted to justify by presuming that risks existed, believing that regulation would mitigate them, and ignoring available alternatives and the costs of their policies. The unfounded search for bank-like risk in asset management had predictable results. Fortunately, the Executive Order presents an opportunity to correct these mistakes and rationalize regulatory structures and authorities. On this front, we believe it makes sense to begin with addressing the FSOC.

Title I of Dodd-Frank created the FSOC and granted it the authority to subject non-bank financial institutions to prudential regulation by the Federal Reserve if the FSOC finds that the financial institution poses a threat to the financial stability of the U.S. economy. SIFI designation authority was highly controversial from the outset. Some viewed it as enshrining the concept of "too big to fail,"[18] while others challenged the decision to task the Federal Reserve with regulating non-banks, which it lacked both the prior experience and in-house expertise to do so effectively.[19] Congress further handicapped the Federal Reserve by requiring it to apply measures that were designed for banks, such as capital requirements, stress testing, the Volcker Rule, and living wills, to non-banks. Unfortunately, after almost seven years, the FSOC has struggled to develop clear standards or sound administrative processes for exercising that authority.[20] FSOC has also ignored

[17] Prudential regulators dominate both the FSOC and FSB. It is interesting to note that the FSOC Member with insurance expertise, Roy Woodall, dissented in both the Prudential and MetLife designations. Missouri Insurance Director John Huff, who was a non-voting member on the FSOC at the time, noted that "some of my fellow FSOC members may not understand the insurance industry," despite the FSOC taking action to designate insurance companies as SIFIs. *See* Elizabeth D. Festa, *FSOC Member: Some Colleagues do not Understand Insurance* (Aug. 23, 2013), http://www.propertycasualty360.com/2013/08/26/fsoc-member-some-colleagues-do-not-understand-insu; *See also* Roy Woodall, *View of the Council's Independent Member Having Insurance Expertise*, http://www.pciaa.net/docs/default-source/industry-issues/views-of-s-roy-woodall-j.pdf?sfvrsn=2 (last visited Apr. 25, 2017).

[18] "To most Americans, the "SIFI" designation process may seem like a classic inside-the-beltway exercise but the stakes are enormous. Designation anoints institutions 'too big to fail.' Today's designations are tomorrow's taxpayer-funded bailouts." House Financial Services Chairman Jeb Hensarling, Opening Statement, Hearing on Financial Stability Oversight Council (May 20, 2014), http://financialservices.house.gov/news/documentsingle.aspx?DocumentID=380567.

[19] *See* Douglas Elliott, Regulating Systemically Important Financial Institutions that are not Banks, Brookings (May 9, 2013), https://www.brookings.edu/research/regulating-systemically-important-financial-institutions-that-are-not-banks.

[20] House Financial Services Committee Staff Report, The Arbitrary and Inconsistent FSOC Nonbank Designation Process, (Feb. 28, 2017), http://financialservices.house.gov/news/documentsingle.aspx?DocumentID=401532; *see also* Letter from Rep. Tom Cotton to Steven Mnuchin, Treas. Sec'y (Mar. 28, 2017), https://www.cotton.senate.gov/?p=press_release&id=646 (urging end to FSOC's Too Big to Fail policies).

multiple recommendations to do basic cost-benefit analyses of the decision to designate a company as a SIFI or to create a framework for analyzing the actual impacts of SIFI designations to determine whether they are actually effective and at what cost.[21]

First, the FSOC focused on money market fund regulation, despite the fact that the SEC, which has primary responsibility for regulating money market mutual funds, was also considering how to address concerns in this market and adopted two rounds of reforms post-crisis. In November 2012, the FSOC voted unanimously to approve a proposal that, if adopted, would allow the FSOC to issue a formal "recommendation" on money market fund regulation to the SEC. While it was not finalized, these actions showed that the FSOC would not hesitate to impose its will on the SEC if its threats were not heeded.

Then in 2013, the OFR published a study, titled *Asset Management and Financial Stability*, which was commissioned by the FSOC.[22] The report, which was strongly criticized by academics, attorneys, former regulators, and the industry, purported to analyze whether and to what extent threats to U.S. financial stability may arise from asset management and whether those threats can (and, if so, should appropriately) be addressed through prudential regulation, or some other regulatory scheme.[23] The answers to those questions were presumed by OFR in the report and by many FSOC members. In fact, neither OFR nor FSOC published the report for comment. The SEC, however, did request public comments.

AMG submitted a letter together with the Investment Adviser Association (the "**IAA**") to the SEC responding to the report. In our comments, we demonstrated that the study lacked evidence of rigorous analysis and did not reflect an accurate or effective understanding of the role of asset managers, the relationship between asset managers and the products they offer, nor presented any facts that link asset managers and investment products to potential financial market distress.[24] SEC Commissioner Daniel Gallagher also publicly criticized the report, observing that "not only did the OFR Report inaccurately define and describe the activities and participants in the asset management business, but it made matters worse by analyzing the purported risks posed by asset

[21] *See* U.S. Gov't Accountability Office, GAO-15-51, GAO Report to the Ranking Member of the Committee on Banking, Housing, and Urban Affairs, U.S. Senate, Financial Stability Oversight Council: Further Actions Could Improve the Nonbank Designation Process (Nov. 2014), http://www.gao.gov/assets/670/667096.pdf.

[22] Office of Financial Research, *Asset Management and Financial Stability* (Sept. 2013), https://www.treasury.gov/initiatives/ofr/research/Documents/OFR_AMFS_FINAL.pdf.

[23] *See* Letter from Committee on Capital Markets Regulation to SEC (Nov. 1, 2013), http://op.bna.com.s3.amazonaws.com/bar.nsf/r%3FOpen%3dcbre-9d2q8r ("Although the OFR Report suggests that funds managed by large asset managers are susceptible to runs and fire sales, it does not provide any empirical evidence that such runs or fire sales pose systemic risk or that such runs or fire sales pose systemic risk or that such runs would occur on asset managers as distinct from funds."); s*ee also* SIFMA AMG Comment Letter to the SEC on Asset Management and Financial Stability (Nov. 1, 2013), http://www.sifma.org/issues/item.aspx?id=8589945983. ("**SIFMA AMG/IAA Letter**").

[24] SIFMA AMG/IAA Letter, *supra* note 23.

managers in a vacuum instead of in the context of the broader markets…[which was] exponentially compounded by OFR's refusal to consider the comments and input from the experts at the SEC."[25]

This report, however, was just "one symptom of a rapidly spreading disease unfairly targeting the asset management industry."[26] At the same time this targeting of asset managers was going on in the United States, the FSB "was engaging in a similar assault on non-bank financial service companies in Basel."[27] Over the years, despite a continued lack of evidence of systemic risk in the asset management industry, AMG has spent a significant amount of time educating and advocating before the FSOC in the United States and FSB and others abroad, as they have continued to search for bank-like risk in an ever widening array of non-bank entities, products, and activities.[28] Throughout the process, regardless of all evidence to the contrary, the FSB and FSOC have continued to "seize[] on bank regulation-oriented concepts as potential indicators of systemic risk transmission mechanisms for investment funds."[29]

By engaging in these deeply flawed reviews, the FSB and FSOC have undermined national securities regulators, who we believe are in the best position to understand the particular nuances of the asset management activities under their authority and engage with industry participants, including through the rulemaking process to design effective and efficient policies. They have also undermined and weakened our capital markets by endeavoring to force a bank-like regulatory construct on the asset management industry and other capital markets participants.

This macroprudential regulatory pressure has, over the years, inappropriately influenced regulation by securities regulators who, heretofore, have focused on implementing and enforcing a principles-based regulatory regime. Now, due to pressure from prudential regulators that one-size-

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[25] Commissioner Daniel M. Gallagher, *Bank Regulators at the Gates: The Misguided Quest for Prudential Regulation of Asset Managers*, Remarks at the 2015 Virginia Law and Business Review Symposium (Apr. 10, 2015), https://www.sec.gov/news/speech/041015-spch-cdmg.html. ("**Gallagher Speech**").

[26] *Id.*

[27] *Id.*

[28] AMG provided written comments to the FSB and the SEC in response to the OFR study and issues relating to separate accounts, as well as comments on the FSB's consultative document, titled *Assessment Methodologies for Identifying Non-Bank Non-Insurer Global Systemically Important Financial Institutions*. In August 2014, AMG also joined several other organizations in petitioning the FSOC to propose amendments to, seek public comment on, and ultimately amend, the FSOC's existing rules concerning the designation of systemically important nonbank financial institutions for supervision by the Board of Governors of the Federal Reserve System. In 2015, AMG submitted comments in response to the FSOC's *Notice Seeking Comment on Asset Management Products and Activities*. We also provided comments to the FSB on the FSB/IOSCO revised proposal, titled *Assessment Methodologies for Identifying NBNI G-SIFIs*, and provided comments to the FSB in response to the request for feedback on the *Peer Review on Implementation on the FSB Policy Framework for Financial Stability Risks Posed by Non-Bank Financial Institutions*. Most recently, in September 2016, we submitted a comment letter in response to the FSB's *Proposed Policy Recommendations to Address Structural Vulnerabilities from Asset Management Activities*. Each of these letters is available on AMG's website, http://www.sifma.org/amg/.

[29] *See* Gallagher Speech, *supra* note 25.

fits-all prudential requirements are right for all entities, securities regulators have hurried to address unfounded concerns of potential systemic risk related to liquidity risk management, data collection, leverage, business continuity planning, and stress testing, again despite a lack of evidence of systemic risk in any of these areas. The proposed (and in certain cases finalized) regulations have included components that are not efficient, effective, or appropriately tailored to the asset management industry.

Additionally, we have reiterated time and again to the FSOC and prudential regulators that asset management activities have not been shown to pose any systemic risks to U.S. or global financial stability.[30] On the contrary, asset management activities are a main stabilizing force in financial markets, facilitating long-term investment in financial assets, distributing risk broadly across asset holders and geographies, and promoting retirement security for millions. Given this unique structure, the regulatory framework for assessing and addressing risk in asset management must therefore be different from the regulatory structure that is appropriate for banks. Essentially, applying to asset management activities prudential standards appropriate only for other industries, such as banking, is tantamount to forcing a square peg into a round hole.

We have also argued to the FSOC and prudential regulators that all regulatory efforts should be based on sound empirical data, rather than hypothetical risks or unsubstantiated claims. Each industry should also be evaluated for its individual structure and risks (or lack thereof). We firmly believe that asset managers should not be subject to prudential regulations that firms operate under when federally subsidized. Yet, we have found that despite the regulators noting, for example, that open-end funds "have not created global financial stability concerns in recent periods of stress and heightened volatility," the FSOC and FSB's unattainable mandate to attempt to predict the next crisis has led the regulators to speculate and go down rabbit holes, in this case arguing that risks must have increased or because asset managers' funds or clients hold some of the same assets that banks do, and therefore prudential regulation may be appropriate notwithstanding the fundamental differences between them.

Need for Recalibration

Core Principles (d), (f), and (g)

AMG supports the FSOC's (and FSB's) role in monitoring and advising with regard to data or regulatory gaps and best practices, as well as promoting coordination and information exchange among authorities responsible for different segments of the financial system. However, the FSOC should not have the ability to designate an asset manager or investment fund as systemically important, subjecting that entity to bank-style oversight by the Federal Reserve.

Despite a lack of evidence by the FSOC and prudential regulators, asset managers have had to continuously defend themselves against these repeated considerations of entity SIFI designations and the accompanying impractical and unfeasible prudential regulatory requirements. These regulatory requirements, including capital requirements, the Volcker Rule, and "living will" plans are clearly inappropriate for the asset management industry.

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[30] See footnote 28 for a complete list of AMG's comment letters to the FSOC, FSB, and IOSCO.

It is irrational for prudential regulators to treat asset managers as if they are banks, undermining the SEC, which has effectively regulated the industry throughout history. Not only has there been little proof that such oversight is necessary, but also the regulatory red tape would significantly increase unnecessary compliance burdens, raisings costs for investors and harming the capital markets. It would impede economic growth and stagnate the capital markets generally, keeping businesses from reaching their economic goals and reducing the ability of investors to save for retirement. Further, under most of the metrics that have been considered, only U.S. based firms and funds would be considered systemically important, thereby reducing the ability of American companies to be competitive with foreign firms in domestic and foreign markets.[31] All of these results are contrary to the Core Principles.

Non-bank SIFI designation is a poorly conceived authority that has been administered even more poorly. In addition to the Senate letter and House report cited in footnote 20 above, there are numerous other assessments of SIFI designation and FSOC exercise of the authority that are equally damning. They include Judge Collyer's opinion overturning the MetLife designation, Roy Woodall's dissents in the Prudential and MetLife designations, multiple GAO reports, and even more comment letters from academics, industry, and think tanks.[32]

Proposed Solutions

Since the authority to designate a non-bank as systemically important stems from Title I of Dodd-Frank, the most appropriate solution to FSOC's overreach would be for Congress to repeal the authority of the FSOC to designate non-bank financial companies as SIFIs. AMG supports the provisions in the Financial CHOICE Act,[33] which not only repeals the FSOC's authority to designate non-bank financial companies as SIFIs, but also "retroactively repeals its previous designations of certain non-bank financial companies, and repeals the FSOC's related authority to designate particular financial activities for heightened prudential standards or safeguards, which includes the power to mandate that an activity be conducted in a certain way or be prohibited altogether."[34] We also recommend that Treasury endorse a repeal of the non-bank SIFI designation authority under Title I of Dodd-Frank.

Pending repeal of the SIFI designation authority, the President's recent Memorandum directs a pause on any further non-emergency SIFI designations until Treasury completes its review of its non-bank systemic risk designation procedures. We fully support this review and urge

[31] *See* Gallagher Speech, *supra* note 25.

[32] *See e.g.,* Roy Woodall, *View of the Council's Independent Member Having Insurance Expertise*, http://www.pciaa.net/docs/default-source/industry-issues/views-of-s-roy-woodall-j.pdf?sfvrsn=2 (last visited Apr. 25, 2017).

[33] H.R. ____, Discussion Draft of the Financial CHOICE Act, https://financialservices.house.gov/uploadedfiles/choice_2.0_discussion_draft.pdf (last visited Apr. 27, 2017).

[34] House Financial Services Committee, *The Financial Choice Act: Creating Hope and Opportunity for Investors, Consumer, and Entrepreneurs* (June 23, 2016), http://financialservices.house.gov/uploadedfiles/financial_choice_act_comprehensive_outline.pdf.

Congress, Treasury and the FSOC to eliminate SIFI designations for non-bank financial institutions permanently. Pending this elimination, we recommend that Treasury completely overhaul the process for considering non-banks under the designation authority to address the fatal transparency and procedural flaws described in the letter from AMG and other trade associations from November 2014 and noted by the House Financial Services Committee and Senate Banking Committee leadership.[35]

In the AMG letter, our members noted significant concerns with the Stage 1 metrics, which rely too heavily on intangible assets or take into account client assets, which are not owned by the asset manager. We also noted concerns with the appeal process and the ability for an asset manager to "off-ramp," which would be largely addressed with increased transparency and engagement with the companies under review. FSOC should at minimum amend Stage 1 criteria to limit the calculation of quantitative metrics to economic assets (excluding goodwill, intangible, and clients assets that are consolidated for US GAAP purposes), increase the transparency of the process, and explicitly establish an off-ramp process if a firm is designated. As part of this process, FSOC should allow a designated firm to create and provide a risk management plan to the FSOC so that the firm may exit the designation.

We support the FSOC continuing to serve as an inter-agency forum, and we support FSOC's Section 120 Dodd-Frank authority to recommend new or enhanced standards for systemic financial services activities to primary regulators, regardless of a company's corporate form or ownership. We believe it is essential for there to be a body that is monitoring market developments and facilitating information-sharing and regulatory coordination on systemic issues. These responsibilities should be the core focuses of the FSOC, rather than wasting time and energy on designations or investigations of entities, products and activities that are already regulated and do not threaten U.S. financial stability.

We also believe it is important for Secretary Mnuchin to recognize officially the benefits of asset management and market-based finance in the Report, as the European Union has done in its Capital Markets Union Initiative.[36] Market-based finance complements banking in terms of powering the economy. Additionally, the FSOC should issue a letter or formal statement acknowledging that its review of asset managers, as well as asset management products and activities, has identified no systemic risks, and explicitly rejecting the macroprudential approach to regulation in this sector. The statement should support the efforts of the SEC to modernize the regulation of asset management, and endorse a repeal of the non-bank SIFI designation authority under Title I of Dodd-Frank.

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[35] *See* SIFMA AMG, American Council of Life Insurers (ACLI), the Financial Services Roundtable (FSR), and the Association of Institutional INVESTORS (AII) letter to the FSOC (Nov. 26, 2014), http://www.sifma.org/issues/item.aspx?id=8589952268.

[36] *See, e.g.*, Jonathan Hill, Member, European Comm'n, Speech at the Finance Watch Conference: Finance at Your Service – Capital Markets Union as an Instrument of Sustainable Growth (Feb. 4, 2015), http://europa.eu/rapid/press-release_SPEECH-15-4144_en.htm; *see also* Sir Jon Cunliffe, Deputy Governor Fin. Stability, Bank of Eng., Speech at the City of London Corporation and Open Europe Conference: Financial Stability, the Single Market and Capital Markets Union (Jan. 20, 2015), http://www.bankofengland.co.uk/publications/Documents/speeches/2015/speech789.pdf.

2. Prudential Requirements Affecting the Capital Markets and Qualified Financial Contracts

While AMG is supportive of strong bank capital requirements, a number of prudential requirements that the federal banking agencies have imposed or have proposed to impose on banking organizations in recent years have negatively affected the capital markets and threatened the ability of AMG members to obtain financial services from banking organizations on behalf of their clients. These prudential requirements, which include the SLR, NSFR, and SCCL, distort the bank's exposure for client transactions and, as a result, have unintended consequences on the market.

In addition, the prudential regulators' restrictions on close-out rights in qualified financial contracts ("**QFCs**") likewise impair the ability of asset managers to enter into financial transactions on behalf of their clients due to the reduction of their clients' contractual protection. These restrictions, if necessary, should be achieved through Congressional action and should be narrowly-tailored to address the cross-border enforceability issues targeted by other jurisdictions.

i. Supplementary Leverage Ratio

AMG members on behalf of their clients use futures, swaps, and other derivatives to manage or hedge investment risks, including interest rates, exchange rates, and commodities. Consistent with clearing requirements predating the financial crisis and additional requirements set forth in Title VII of the Dodd Frank Act, many liquid, standardized derivative contracts are generally cleared through central counterparties ("**CCPs**") commonly referred to as clearing houses, with end users acting through futures commission merchants ("**FCMs**") that are members of CCPs. Most FCMs are subsidiaries of banking organizations. AMG members and their clients rely on FCMs for access to cleared derivatives markets to hedge risks in their clients' portfolio.

As part of the Basel III framework, the Basel Committee on Banking Supervision ("**BCBS**" or "**Basel Committee**") and U.S. federal banking regulators imposed a new leverage ratio capital requirement on banking organizations, called the SLR in the United States. While denominators of leverage ratios have traditionally captured a banking organization's total assets, the denominator of the SLR extends for the first time to ***off***-balance sheet exposures, such as the guarantee that a banking organization, typically through an FCM subsidiary, provides to a CCP when acting as agent in a client cleared derivative transaction. In calculating the exposure arising out of the FCM's guarantee to the CCP, the denominator of the SLR does not take into account the initial margin that the client provides the FCM, which the FCM is required to segregate by law from its own proprietary assets, and which reduces the FCM's ***actual economic exposure*** arising out of the guarantee. As a result, the SLR needlessly overstates a banking organization's exposure from its client cleared derivative transactions.

In the United States, this problem is compounded by the fact that the SLR is more stringent than the leverage ratios of other jurisdictions in at least two ways, which places the U.S. markets and market participants at a distinct disadvantage:

- First, the European Commission released a leverage ratio proposal in November 2016 that, unlike the U.S. SLR, would recognize the exposure-reducing effect of customer initial margin provided to a banking organization in a client cleared derivative transaction.

- Second, the Basel Committee set the international leverage ratio requirement at 3 percent, but the federal banking agencies gold-plated the international standard in the U.S. by implementing an "enhanced" SLR that requires the eight U.S. global systemically important banking organizations ("**G-SIBs**") to maintain an additional layer of 2 percent of Tier 1 capital to avoid being subject to restrictions on their capital distributions and discretionary bonus payments. Thus, the U.S. G-SIBs will effectively be required to maintain an SLR of ***5*** percent. Insured depository institutions subsidiaries of U.S. G-SIBs will be required to meet a ***6*** percent SLR to be deemed "well capitalized." This heightened requirement increases the possibility that for at least some U.S. G-SIBs, the SLR will be their binding capital constraint and will be the primary driver of their capital allocation decisions.

The SLR will become effective as a minimum requirement on January 1, 2018, and banking organizations have been required to disclose their SLRs publicly since January 1, 2015.

Need for Recalibration

Core Principles (d) and (f)

The SLR is unnecessarily increasing costs to investors and unduly reducing access to markets for a number of clients. Banking organizations allocate capital to business lines based on their risk-adjusted return-on-equity ("**ROE**"), and consider derivatives clearing to be a low-risk, low-return business. Because the SLR requires banking organizations to maintain much more capital to support the derivatives clearing business than is suggested by the returns of the business, banking organizations have begun to respond to the SLR by exiting the business, off-boarding clients, and/or raising prices.

Even as a disclosure-only standard until 2018, the SLR has already caused increases in clearing fees and losses in access to cleared derivatives for hedging purposes as banking organizations seek to reduce their total leverage exposure (the denominator of the SLR). According to an AMG member survey, following the introduction of the SLR, 60 percent of survey respondents have been asked to pay higher clearing fees for interest rate swaps, 50 percent of respondents have been asked to "cap" the notional amount of their interest rate swaps outstanding with a clearing member, and 30 percent of interest rate swap users have been forced to terminate relationships with clearing member (and seek clearing services elsewhere, if possible).[37] We believe

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[37] AMG conducted the survey as of June 21, 2016, and twelve AMG members, representing an aggregate of over $1 trillion in assets under management, participated. More detailed survey results are available in our

these adverse effects on AMG members and their clients will become even more pronounced as the January 1, 2018 effective date of the SLR minimum requirement approaches. For instance, after the AMG member survey was completed, Deutsche Bank decided to exit the U.S. swaps clearing market due to the SLR,[38] and we fear that U.S. banking organizations will soon do the same, which would undermine the competitiveness of the U.S. capital markets and disadvantage U.S. asset managers and their clients.

Proposed Solutions

The federal banking agencies should revise the denominator of the SLR to recognize the exposure-reducing effect of segregated assets initial margin provided to the banking organization in client cleared derivative transactions. This collateral is treated by banking organizations as client assets, and a significant portion is on-posted to the CCPs. The agencies should also reduce the enhanced SLR requirement for some of the U.S. G-SIBs, as former Federal Reserve Board Governor Daniel K. Tarullo recently suggested doing.[39] Because the SLR and enhanced SLR are not required by statute, the agencies can take both these steps without legislative action.

ii. Net Stable Funding Ratio

The NSFR is a liquidity standard originated by the Basel Committee that requires banking organizations to use long-term funding, which is more expensive than short-term funding, to support certain balance sheet activities that regulators have deemed to present liquidity risk. The NSFR categorizes the stability of a bank's funding sources using an "Available Stable Funding" ("**ASF**") score, and categorizes the liquidity risk of a bank's assets and activities using a "Required Stable Funding" ("**RSF**") score.

The development of the NSFR has been plagued with issues from the beginning, and demonstrates the pitfalls of allowing U.S. regulation to be dictated by an international body. The Basel Committee issued a series of NSFR proposals from 2009 to 2014, but in October 2014, issued a final standard that included a number of key new provisions that had never been subject to public consultation, including provisions that overstate the liquidity risk of derivatives, repo, and securities financing transactions, and did not release any data to support these provisions. AMG members have a particular interest in these provisions because AMG members enter into derivatives, repo, and securities financing transactions to hedge risks in their clients' portfolio and implement their investment strategies.

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comment letter to the Basel Committee. *See* Letter from SIFMA AMG to the Basel Committee on Banking Supervision (June 30, 2016), http://www.sifma.org/issues/item.aspx?id=8589961201.

[38] *Deutsche Bank Is Said to Close U.S. Swaps-Clearing Business*, Bloomberg (Feb. 8, 2017), https://www.bloomberg.com/news/articles/2017-02-09/deutsche-bank-is-said-to-close-u-s-swaps-clearing-business.

[39] *See* Remarks by Federal Reserve Board Governor Daniel K. Tarullo, Departing Speech (Apr. 4, 2017), https://www.federalreserve.gov/newsevents/speech/tarullo20170404a.htm.

The federal banking agencies issued a proposed rule in 2016 to implement the NSFR in the United States for large banking organizations.[40] Not only did the federal banking agencies' proposed rule include the elements of the international standard that had never been subject to public comment, the agencies also proposed to gold-plate the international standard in certain ways.

While the federal banking agencies hastened to implement and gold-plate the flawed international standard, the European Commission released a proposal in November 2016 that would provide significantly more favorable treatment to certain types of transactions, including derivatives and repo, than the international standard.[41]

Need for Recalibration

Core Principles (d) and (f)

We have serious concerns that the federal banking agencies' NSFR proposal would produce very little additional prudential benefits beyond those resulting from the many new regulations adopted since the financial crisis, while at the same time it could impose material costs on banking organizations entering into derivative, repo, and securities financing transactions with asset managers. Banking organizations will pass these costs on to our members' clients – ultimately to the detriment of retirement savers, retail investors, corporations, and consumers.

Proposed Solutions

The federal banking agencies should withdraw the NSFR proposal. If they do decide to finalize the NSFR, however, they should re-release a proposal for public comment along with data supporting the proposal. If re-proposed, the NSFR could stand to be improved in several respects. Our specific, technical suggestions are discussed in a comment letter to the federal banking agencies,[42] and include:

- ***Tailoring the Criteria for Recognition of Variation Margin to the NSFR Context.*** The final NSFR should (1) permit broader categories of assets for variation margin to reduce a banking organization's derivative asset amounts, (2) permit variation margin denominated in any currency of a jurisdiction in which the banking organization operates to reduce derivative asset amounts, and (3) permit variation margin to reduce derivative asset amounts even if it is not the full amount necessary to extinguish the banking organization's current exposure.

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[40] Net Stable Funding Ratio: Liquidity Risk Measurement Standards and Disclosure Requirements, 81 Fed. Reg. 35123 (proposed June 1, 2016) (to be codified at 12 C.F.R. pts. 50, 249 and 329).

[41] European Commission Proposal COM(2016) 850 final (Nov. 23, 2016), https://ec.europa.eu/transparency/regdoc/rep/1/2016/EN/COM-2016-850-F1-EN-MAIN.PDF.

[42] Letter from SIFMA AMG to Federal Reserve System, et al. on Proposed Net Stable Funding Ratio Requirement (Aug. 5, 2016), http://www.sifma.org/issues/item.aspx?id=8589961796.

- ***Providing a Downward Adjustment to the RSF Factors of Derivatives With a Short Remaining Maturity.*** The final NSFR should recognize that short-dated derivative assets require less stable funding by including downward adjustments for derivatives with a remaining maturity of one year or less and six months or less.

- ***Releasing More Information Relating to the Add-On for Potential Derivative Portfolio Valuation Changes.*** The agencies should release their data supporting the proposed add-on for derivative portfolio valuation changes, and explain how the add-on bears a reasonable relationship to the risk it seeks to capture. At the very least, the final U.S. NSFR should not gold-plate the Basel NSFR standard by grossing up settlement payments that extinguish a banking organization's obligation to its counterparty for purpose of calculating the add-on.

- ***Treating Repo and Reverse Repo Symmetrically.*** The agencies should assign the same percentage factors to the ASF of repos and the RSF for reverse repos for financial sector entity counterparties so as not to disincentivize matched book funding and disrupt the functioning of capital markets transactions that depend on banking organizations to provide repo funding.

- ***Recognizing Assets and Liabilities Associated With Client Shorts as Interdependent Assets and Liabilities Requiring 0 Percent RSF or ASF.*** The agencies should use the discretion permitted to them under the Basel standard to assign a 0 percent RSF to assets arising out of client short transactions when the banking organization's role in the securities borrowing transaction is subject to Regulation T.

- ***Assigning a 0 Percent RSF Factor to Segregated Client Assets.*** The final NSFR should treat client assets subject to strict SEC or CFTC segregation requirements as the client's property, requiring no stable funding by the banking organization.

The NSFR is not required by statute. Accordingly, the federal banking agencies do not need legislative action to determine not to finalize the NSFR, or to revise the proposed NSFR substantially.

iii. Single-Counterparty Credit Limits

The Federal Reserve issued proposals in 2011 and 2016 to implement the SCCL for banking organizations with $50 billion or more in assets (known as "**covered companies**") as required under Dodd-Frank. The 2016 proposal would require covered companies to quantify their aggregate exposures to counterparties across business lines and subsidiaries and keep those aggregate exposures within specified quantitative limits. In implementing the SCCL, there are three critical issues for AMG members: (1) defining what entities are part of the covered company, (2) defining what entities form a single counterparty and how a covered company is to make such a determination, and (3) determining how exposures are to be calculated.

Need for Recalibration

Core Principles (f)

AMG members have concerns about the 2016 proposal from their perspective as counterparties to covered companies, and for some members, also from their perspective as affiliates of covered companies. Our concerns fall into three categories:

- The 2016 proposal includes an overly broad definition of "covered company" that includes any entity that a top-tier bank holding company "controls" under the Bank Holding Company Act ("**BHCA**"). The term "control" has been interpreted expansively by the Federal Reserve, and could sweep in investment funds (1) advised, sponsored, or managed by an asset management subsidiary of a bank holding company, even though those funds do not necessarily expose the covered company to losses, and (2) in which the bank holding company has a substantial minority investment, but no practical ability to force to comply with the covered company's exposure limits. We believe it is unnecessary to sweep in these types of funds as part of the covered company to accomplish the purposes of the SCCL.

- The 2016 proposal also includes a requirement that a covered company aggregate multiple entities as a single "counterparty" if the entities are connected by controlling relationships. This control aggregation test would impose serious burdens on investment funds that seek to establish and maintain relationships with covered companies. To establish whether multiple entities are related such that they should be considered a single counterparty, the covered company would be required to request competitively sensitive, proprietary, and/or personal information from the entities; this information could be subject to information barriers due to other regulatory requirements.

- The 2016 proposal would require any covered company to calculate its exposures to certain investment funds using a "full look-through approach," in a manner that would overstate the covered company's actual economic exposure, and also would impose excessive burdens on covered companies and their counterparties to perform the calculation.

Proposed Solutions

Our specific, technical suggestions are discussed in more detail in a comment letter to the Federal Reserve,[43] and include:

- ***Definition of "covered company."*** The final SCCL rule should define "covered company" to include the top-tier bank holding company and all entities consolidated with the bank holding company for financial reporting purposes except for (a) investment funds sponsored by the bank holding company or any of its affiliates, and (b) portfolio companies of the bank holding company held under the merchant banking authority of section 4(k) of the BHCA.

- ***Definition of "counterparty."*** The final SCCL rule should define "counterparty" only to include, with respect to a company, the company and all persons that that counterparty consolidates for financial reporting purposes. In addition, the rule should not include a control aggregation test. At a minimum, the final SCCL rule should include a *de minimis* threshold for control aggregation.

- ***Exposures to investment funds.*** The final SCCL rule should clarify that only equity or equity-like exposures of a covered company to an investment fund require the use of the full look-through approach. The rule should require a covered company to calculate its exposures to the underlying assets of an investment fund on a full look-through basis only if the covered company cannot demonstrate that its exposure to the fund is less than 5 percent of the covered company's Tier 1 capital.

The Federal Reserve can make these changes in the final SCCL rule without legislative action. If the Federal Reserve does not address these issues, we believe the costs of the final SCCL rule would exceed its benefits, and the rule would be inconsistent with the Core Principles.

iv. Restrictions on Qualified Financial Contracts

Beginning in 2013, prudential regulators in the U.S., Europe and Asia with 18 major global banks ("**G-18**") and other banks and market participants considered cross-border enforceability issues for Special Resolution Regimes ("**SRRs**") in respect of QFCs, particularly QFCs entered into by a bank in one jurisdiction with a governing law provision that selects another jurisdiction. In 2014, the G-18 developed a protocol to amend terms of over-the-counter ("**OTC**") swap agreements (a type of QFC) amongst the G-18 such that SRR restrictions, or "stays" on the right to exercise termination rights would apply irrespective of governing law provisions. Prudential regulators sought expansion of this protocol to additional QFCs—specifically, repurchase agreements and securities lending agreements—and additional counterparties, including asset managers' clients. The latter expansion to asset managers' clients has been effectuated in

[43] Letter from SIFMA AMG to Robert deV. Frierson, Sec'y, Bd. Of Governors, Fed. Res. Sys. on the SCCL Proposal (June 3, 2016), http://www.sifma.org/issues/item.aspx?id=8589960701.

jurisdictions outside of the U.S. through regulations and laws, which, in turn, have been implemented through contractual changes.

Regulations proposed by the U.S. federal banking agencies—specifically, those proposed by the Federal Reserve,[44] OCC,[45] and the FDIC[46]—imposed restrictions far beyond cross-border enforceability of the U.S. SRR (i.e., Title II of the Dodd Frank Act), going far beyond the issues addressed in other jurisdictions. The federal banking agencies' proposals included restrictions on QFCs governed by New York law and cross-default rights in ordinary bankruptcy.

Need for Recalibration

Core Principles (d) and (f)

The federal banking agencies' proposed rules on the cross-border enforcement of the U.S. SRR (i.e., Title II of the Dodd Frank Act) would be best addressed through Congressional action. AMG understands the objective of securing cross-border recognition of U.S. SRRs but does not believe that prudential rules that apply to banks, and only indirectly to market participants through contractual restrictions, are the best means to address policy decisions that impact important rights of investors.

Although the FSB's Principles for Cross-Border Effectiveness of Resolution Actions recognized that "properly crafted and widely adopted [] contractual recognition approaches offer a workable solution until comprehensive statutory regimes for giving cross-border effect to resolution action are adopted,"[47] the federal banking agencies' proposals are not narrowly tailored to operate as that sort of stop-gap measure. Instead, they would apply to all QFCs, including those governed by U.S. laws, and would apply irrespective of whether the QFC terms provide for default rights. The proposed rules' requirements regarding QFC recognition of U.S. SRRs' restrictions on default rights are based on the term "QFC" as that term is broadly defined in Title II of Dodd-Frank.

Further, the proposed rules impose restrictions on certain investor rights in an ordinary bankruptcy, beyond application of the U.S. SRR—specifically, cross-default rights (i.e., rights to terminate a QFC due to an affiliate of a covered entity counterparty becoming subject to an insolvency proceeding). Such agreed cross-default rights bear an important relationship to guarantees that may be provided, and they relate to credit assessments that include the parent or affiliate(s) of the counterparty. AMG does not believe that these rights should be restricted and represent, in effect, an unwarranted change to existing statutory standards. The proposed rules' requirements to restrict cross-default rights contractually would represent, in effect, an unwarranted

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[44] 81 Fed. Reg. 29169 (May 11, 2016) ("**Fed QFC Proposal**").

[45] 81 Fed. Reg. 55381 (August 19, 2016).

[46] 81 Fed. Reg. 74326 (October 26, 2016).

[47] FSB, *Principles for Crossborder Effectiveness of Resolution Actions* (November 3, 2015) at 5, http://www.fsb.org/wp-content/uploads/Principles-for-Cross-border-Effectiveness-of-Resolution-Actions.pdf.

change to existing statutory standards. The Federal Reserve in its proposal acknowledges that U.S. SRR proceedings, which trigger certain limited statutory restrictions upon the exercise of cross-default rights, will be "used rarely" under "extraordinary circumstances." The Federal Reserve further acknowledged that, in contrast, upon the filing of an ordinary bankruptcy, "[t]he Bankruptcy Code's automatic stay … does not prevent the exercise of cross-default rights against an affiliate of the party entering into resolution."[48] Despite the clear statutory difference intended by Congress for the different circumstances, the federal banking agencies' proposals would require covered entities to contractually agree that cross-default rights under QFCs cannot be exercised in connection with the *non-extraordinary* event of a bankruptcy proceeding. The Federal Reserve's stated intention is "to address . . . obstacles to orderly resolution under the Bankruptcy Code *by extending* [Dodd-Frank's Title II orderly liquidation authority] stay-and-transfer provisions to any type of resolution of a covered entity."[49]

AMG does not believe that a material alteration of the ability of counterparties to obtain and enforce cross-default rights, taking in to account the existing statutory bankruptcy regime, should be accomplished by rulemakings of the federal banking agencies. The alteration of rights in ordinary bankruptcy is particularly concerning where the disadvantaged counterparties in question, including asset managers' clients, are not supervised by the federal banking agencies. Thus, the approach in these proposals, imposing restrictions on the contractual rights of market participants that are *not* subject to prudential supervision, results in a lack of due consideration of those market participants' interests. While, for example, the Federal Reserve's basic mission statement includes the protection of "credit rights of consumers"[50] – in other words, the Federal Reserve must establish *minimum* standards of conduct related to the maintenance and protection of credit rights of individuals that deal with Federal Reserve-supervised financial institutions – the proposed rules would materially *reduce* available rights of counterparties when they deal with Federal Reserve-supervised financial institutions. The federal banking agencies should not use their rulemaking power to limit creditor protections in a manner that exposes such a broad range of individuals to additional risk.

In addition, the proposed changes to rights in ordinary bankruptcy could result in pro-cyclical behavior as asset managers may be forced to move funds away from covered entities upon the earliest signs of potential financial distress. AMG members have traditionally negotiated and obtained, on behalf of their clients, important rights to protect clients against deteriorating dealer credit. Those rights would be materially limited under the proposals. Accordingly, AMG members may seek exits from trading relationships sooner than they would have if they had been permitted to retain a fuller set of rights on behalf of clients related to contract termination, collateral and other credit-related matters. Such trading decisions could accelerate adverse market conditions in a procyclical fashion, leaving authorities less flexibility and fewer options than anticipated.

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[48] Fed QFC Proposal at 29173.

[49] Fed QFC Proposal at 29179 (emphasis added).

[50] Federal Reserve Board, *Mission*, https://www.federalreserve.gov/aboutthefed.htm (last update: Nov. 6, 2009).

Proposed Solutions

AMG believes that Congress, rather than the federal banking agencies, should take steps to secure cross-border recognition of Title II of Dodd-Frank. To ensure the enforceability of QFCs governed by non-U.S. law entered into by a covered entity, Congress should work with other countries to achieve mutual recognition of all special resolution regimes, including the U.S. SRR, irrespective of the contract's governing law. Absent an agreement on mutual recognition, the U.S. should address the issue through statutory change, not prudential regulation. Indeed, the FSB's Principles for Cross-Border Effectiveness of Resolution Actions "emphasized the importance of implementing comprehensive statutory frameworks" to achieve legal certainty for cross-border resolutions.[51] Given the importance of the contractual rights at issue for pension funds, mutual funds and other investment vehicles held by retail investors, AMG believes that the U.S. prudential regulators should not finalize the proposed rules.

Any steps taken to address cross-border recognition of the U.S. SRRs should be narrowly tailored to achieve that result without impacting rights under domestic law and in ordinary bankruptcy.

B. SEC Regulation of Asset Management Products and Services

Largely as a result of the pressure being placed on the SEC and other securities regulators by the prudential regulators and systemic risk bodies, former SEC Chair White gave a speech in December 2014 titled *Enhancing Risk Monitoring and Regulatory Safeguards for the Asset Management Industry*.[52] In the speech, Chair White began by describing the SEC's rich regulatory history since the passage of the Advisers Act and the 1940 Act. She went on to describe how the industry has evolved over the years, and how the SEC's regulatory tools have responded to the industry's changes. She argued that "a broader set of proactive initiatives is required to help ensure that [the SEC's] regulatory program is fully addressing the increasingly complex portfolio composition and operations of today's asset management industry. She explained that the SEC staff, at her direction, was in the process of developing recommendations for three core initiatives to (1) improve data collection; (2) enhance fund-level controls in areas such as liquidity and leverage; and (3) ensure firms have a plan for transitioning client assets when circumstances warrant it.

Unsurprisingly, these were the same areas under consideration by the FSOC, as evidenced by the FSOC releasing its Consultation on asset management products and activities, which covered the same issues, later that month.[53] Since Chair White's speech, the SEC has released and finalized

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[51] *Id.*

[52] Mary Jo White, Chairwoman, SEC, Speech to the New York Times DealBook Opportunities for Tomorrow Conference (Dec. 11, 2014), https://www.sec.gov/news/speech/2014-spch121114mjw.

[53] See Financial Stability Oversight Council, *Update on Review of Asset Management Products and Activities*, https://www.treasury.gov/initiatives/fsoc/news/Documents/FSOC%20Update%20on%20Review%20of%20Asset%20Management%20Products%20and%20Activities.pdf (which noted that the FSOC is focused on addressing liquidity and redemptions; leverage; operational functions; securities lending; and resolvability and transition planning) (last visited Apr. 27, 2017).

regulations on data collection and liquidity risk management. They have also issued proposed regulations on leverage/use of derivatives and business continuity planning/transition planning, and publicly considered, though not yet proposed, regulations on stress testing.

AMG supported most of the SEC's efforts, as the industry's primary regulator, and commented to SEC staff on how they could improve the proposals. The only regulations that have been finalized – data collection and liquidity risk management – were improved from the proposal stage to the final regulation, but each regulation was clearly and significantly negatively impacted by the influence of the FSOC and other prudential regulators. As a result, none of the regulations either proposed or finalized meet the standard outlined in the Core Principles that regulations must be efficient, effective, and appropriately tailored. Each of these regulations is discussed below.

1. Stress Testing

Section 165(i) of Dodd-Frank provides that "a nonbank financial company supervised by the [Federal Reserve] and a bank holding company described in subsection (a) shall conduct semi-annual stress tests. All other financial companies that have total consolidated assets of more than $10 billion and are regulated by a primary Federal financial regulatory agency shall conduct annual stress tests."[54] The SEC has interpreted this provision to mean that it must draft a rule to require stress testing of registered investment advisers and funds, each with $10 billion or more in assets, and the staff in the investment management division has been reportedly working on a rulemaking for the last few years, which has not been released. Additionally, in its recent Recommendations, the FSB recommended not only that stress tests be applied to funds and advisers, but also that authorities consider "system-wide stress testing that could potentially capture effects of collective selling by funds and other investors on the resilience of financial markets and the financial system more generally."[55]

AMG strongly disagrees with the premise behind requiring asset managers or funds to follow prescriptive stress testing requirements, and we also disagree with FSB's belief that system-wide stress tests will yield helpful results. There is a conceptual problem with the notion of stress testing the adequacy of a mutual fund similar to a bank, given that mutual funds sell shares at a variable net asset value calculated daily and must comply with SEC rules that strictly limit borrowing and require funds to hold many times more capital (as a proportion of the balance sheet) than even the most strictly regulated bank. These conceptual problems are compounded by the failure to define the objectives and methods of testing, and the failure to consider the costs and benefits to American investors, economic growth, and financial stability. Traditional prescriptive stress testing is typically used in the context of banks, whose balance sheets are assessed to determine whether they have sufficient capital to withstand various economic stress scenarios. Asset managers and funds, in contrast, operate with little or no leverage and are insensitive to many of the macroeconomic factors

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[54] Section 165(i), H.R. 4173 — 111th Congress: Dodd-Frank Wall Street Reform and Consumer Protection Act." 2009, https://www.govtrack.us/congress/bills/111/hr4173 (last visited Apr. 25, 2017).

[55] Financial Stability Board, *Policy Recommendations to Address Structural Vulnerabilities from Asset Management Activities* (Jan. 12, 2017), http://www.fsb.org/wp-content/uploads/FSB-Policy-Recommendations-on-Asset-Management-Structural-Vulnerabilities.pdf.

that impact a bank's financial health and did not require a safety net during the financial crisis. As with SIFI designations, this is a "solution" in search of a problem.

Further, to require bank-like stress tests on open-end funds reflects a central misunderstanding of the critical differences between the risk profiles of a bank and a mutual fund. When a bank fails or depositors lose the value of their deposits that exceed insured amounts, borrowers lose access to a source of capital. This, in turn, causes the amount of money and credit available in the markets to decline, creating the potential for systemic shock and pressuring government safety nets that support banks. Stress testing a bank consists of assessing its total balance sheet risk – its capital relative to its assets and exposures to creditors, borrowers, and counterparties. In contrast, when a mutual fund closes (or fails, which is a rare occurrence) or an asset manager ceases to provide investment advisory services to a fund, an investor's assets may be transitioned to a new fund or a new asset manager without creating a negative ripple effect on the financial markets. A mutual fund investor, not the fund or the asset manager or the relevant government, knowingly and willingly bears the market risk of his or her investment. The investor has no expectation that the FDIC or any other insurance will offset that risk; all mutual fund prospectuses bear disclosure of that fact, and investors know that their funds are not on deposit but rather are being invested with an agreed level of risk.

We agree with SEC officials, like former Chief Economist Mark Flannery, who argued that the SEC's potential rulemaking for funds and managers is based on a "false parallel" that stress testing asset managers will function like stress testing large banks.[56] We also believe that it is unnecessary, given the SEC's regulations related to liquidity risk management, which essentially requires stress testing by setting out specific factors that must be considered as part of the liquidity risk management program. To go beyond these requirements and implement prescriptive, bank-style stress tests would make the system less safe in practice, because the industry would naturally become more homogenous, and all asset managers would behave similarly to one another in times of stress. Ultimately, this rule will be costly to implement, and yield little or no useful information, while making the system less safe.

Similarly, there are conceptual problems with the notion of implementing system-wide stress tests, as suggested by the FSB. The suggestion to stress test the system is based on the fear that a market event could incite redemptions across a particular sector, which might in turn force funds to sell their holdings at once, resulting in fire sales. It is also based on the belief that system-wide stress tests would yield a comprehensive set of data from which to glean results that speak to the asset management industry's capacity for maintaining (or detracting from) financial stability. Both assumptions are wrong. It is nothing more than an unsubstantiated theory that funds would sell their holdings at once. There is no evidence of this throughout history. Industry data demonstrates that fund shareholders have not behaved in this way and there is less reason, not more, to believe that they might behave in that way in the future.[57] And, the relative size of the asset management

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[56] Rob Tricchinelli, *SEC Vexed by Asset Manager Stress Test Rule*, Bloomberg (Feb. 8, 2016), https://www.bna.com/sec-vexed-asset-n57982067065.

[57] Letter from Paul Schott Stevens, President & CEO, ICI, to Jonah Crane, Deputy Assistant Sec'y, FSOC (July 18, 2016), https://www.ici.org/pdf/16_ici_fsoc_ltr.pdf.

industry would ensure that the regulators would be using incomplete data, because only about one quarter's worth of the total financial assets are managed by the asset management industry, thereby undermining any inferences drawn from system-wide stress tests results.[58]

Need for Recalibration

Core Principles (f) and (g)

Bank-like stress testing for asset managers and funds (other than money market funds) is a prime example of attempting to inappropriately apply a banking tool to the asset management industry. Prescriptive rules in this area would either push the industry to view the world from the same lens, thereby potentially increasing risk in the system, or would yield unrealistic results that do not accurately reflect how fund shareholders or other investors would behave or any given fund would respond to changes in asset liquidity and redemptions during stressed markets.

Further, additional stress test requirements at the manager, fund, or system-wide level would directly materialize into increased shareholder costs. Given that mutual funds are the low-cost investment vehicle of choice for millions of investors, any consideration of stress testing requirements should take into consideration the compounded costs for investors and diminished retirement savings, which we believe would not be offset with added benefit to the health of the asset manager, fund, or the global markets.

Proposed Solutions

Congress should repeal Section 165(i) of Dodd-Frank. The Financial CHOICE Act would address the majority of our concerns by strictly limiting Section 165 to bank holding companies with $50 billion or more in consolidated assets.[59]

Until Congress passes legislation, we urge Treasury to recommend in the Report that the SEC refrain from implementing any additional stress testing requirements on asset managers, funds, or the financial system until the requisite research is completed in this basically uncharted area, or Congress addresses the issue through legislation. We also urge Treasury to recommend that IOSCO delay its work related to FSB's recommendations on stress testing until additional research is completed and the United States determines what efforts, if any, would be in the best interests of individual investors, the capital markets, and the U.S. economy.

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[58] Blackrock Viewpoint, *Macroprudential Policies and Asset Management* (Feb. 2017), https://www.blackrock.com/corporate/en-us/literature/whitepaper/viewpoint-macroprudential-policies-and-asset-management-february-2017.pdf (the viewpoint also notes, among other things, that if policymakers use system-wide stress tests to justify policies that artificially prop up prices by restricting the sale of downgraded assets, they are more likely to create asset price bubbles and severe distortions than to mitigate systemic risk.).

[59] Dodd-Frank also directs all financial regulatory agencies to write rules regarding stress testing. *See* Dodd-Frank Wall Street Reform and Consumer Protection Act § 165, 12 U.S.C. § 5365. While not addressed by the first version of the Financial CHOICE Act, this sentence should also be struck when Congress addresses these concerns by legislation.

2. Data Collection Requirements

On October 13, 2016, the SEC adopted final rules that substantially increased the amount, frequency, and public availability of data that SEC registered funds will be required to report to the SEC.[60] Among other new data sets that will be reported, an entirely new form, Form N-PORT, will require:

- Monthly reporting in structured format for each individual fund or series;
- Detailed portfolio holdings information, on a holding by holding basis (including numerous prescribed fields for each type of investment); and
- Prescribed risk metric data, at both the individual holding and portfolio level.

The SEC and its high-level staff have described the new data reporting requirements as "transformative" and a "game-changer," in terms of the amount of data the agency will be collecting. Form N-PORT will replace a current form that is filed only on a quarterly basis, and calls for a much more limited and streamlined set of portfolio holdings information.[61]

In the same rulemaking, the SEC adopted comprehensive revisions to accounting rules for funds, Regulation S-X, which will require funds to include in their financial statements standardized schedules containing information about their derivatives investments and additional information about securities lending activities; and a new annual census report, Form N-CEN, which will replace an existing outdated form and substantially expand the amount and type of data required. The SEC also proposed, but did not adopt, a rule (Rule 30e-3) that would have reduced costs and burdens currently incurred by funds in connection with delivering shareholder reports, which is discussed in further detail in the next section.

Additionally, on August 25, 2016, the SEC adopted amendments to its reporting form for SEC registered investment advisers (Form ADV), which will now will require advisers to provide substantial information about their separately managed account business.[62]

AMG supported the SEC's decision to take the initiative in modernizing its data collection requirements in the face of developments in financial markets, technology, and global regulation. However, we identified certain proposed requirements where we believed the burdens of reporting would not produce commensurately beneficial information. Most importantly, we asked the SEC to reconsider its decision to make virtually all of the new required data available to the public, on a quarterly basis (with a 60 day lag). We expressed grave concern that public availability of these enormous amounts of detailed data, in structured format, would both pose the threat of substantial harm to proprietary information and undermine the carefully developed current investor disclosure regime.

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[60] Investment Company Reporting Modernization, 81 Fed. Reg. 81870 (Nov. 18, 2016).

[61] Carmen Germaine, *SEC Adopts 'Transformative' Rules For Mutual Funds*, Law360 (Oct. 13, 2016), https://www.law360.com/articles/850865/sec-adopts-transformative-rules-for-mutual-funds.

[62] Form ADV and Investment Advisers Act Rules, 81 Fed. Reg. 60417 (Sept. 1, 2016).

The SEC rejected our arguments both about the harm posed by public availability of the new data and the specific items we considered to be reporting overkill, with very minor exceptions. The SEC also rejected AMG's request that they address the duplication between the reporting requirements to the SEC and the CFTC, such as ensuring that there would be "substituted compliance" between Form CPO-PQR, the reporting form for commodity pool operators registered with the CFTC, and new Form N-PORT. For the most part, with the exception of dropping Rule 30e-3 (a cost-reducing proposal) from the initiative, the SEC adopted the reporting rules as proposed.

Need for Recalibration

Core Principles (f) and (g)

The final data regulations are not efficient, effective, or appropriately tailored to the asset management industry. Significant harm will likely result from the public disclosure of the information that will be obtained by the SEC on Form N-PORT, including enabling of such predatory practices as front-running, copycatting, and reverse engineering of a fund or manager's investment strategy. This is particularly true, given that the data on the new form will be in a structured data format, which will make reverse engineering and attempts to glean manager strategy far easier than in the past.

The potential for these harms to materialize is also not outweighed by countervailing benefits. Public availability of the new data is not necessary to achieve the primary goal of the data modernization rules – to improve regulatory oversight. And, while we share the goal of improving investor decision making through meaningful disclosure, Form N-PORT does not accomplish that goal, and indeed undermines it. The massive fields of fragmented data elements required by the Form are designed primarily for the SEC's regulatory purposes. Providing these data sets to investors (either directly or filtered for them by vendors and other intermediaries) without any context for understanding or weighing the significance of the individual items, will at best be of little value to fund investor decision making.[63] At worst, and in our view far more likely, this new data will harm investor decision making by distracting investors from the prospectus disclosure requirements the SEC has specifically designed to provide fund investors with the information they need. Public availability of Form N-PORT information on a quarterly basis, therefore, is likely to result in misleading, or at a minimum confusing, individual investors. The SEC would better protect investors by requesting and obtaining information tailored to its regulatory needs, on a non-public basis, than by making that information publicly available.

In accordance with the Core Principle seeking to rationalize the Federal financial regulatory framework, the SEC's data collection rulemakings (as well as the CFTC's and that of any other

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[63] It should be noted that data on Form N-PORT will be reported in a structured data format that requires special tools to view and decipher. Thus, it is highly likely that any retail investors who seek access to this data will do so through intermediaries (such as Morningstar) rather than directly. These intermediaries are unlikely to offer this data for free—thus, the data on Form N-PORT, while publicly available in a technical sense, will practically be available only to those retail investors who pay fees to access it. This disparity in access to "public" data by retail investors also argues strongly in favor of making the data non-public.

regulatory agency that issues regulations that affect asset managers) should also prioritize efficiency and coordination with other regulatory bodies. At present, reporting requirements among the various regulatory agencies are duplicative and confusing, without standardized terminology or in many cases appropriate substituted compliance regimes. Addressing these issues would significantly improve the financial regulatory framework and limit unnecessary costs and burdens, which directly affect retail and institutional investors.

Additionally, the pilot programs underway at the OFR for securities financing transaction ("SFT") include reporting requirements, which OFR would like to make permanent, that are duplicative with the new SEC reporting requirements. To the extent they are not duplicative, they ask for significant information beyond what is required by international standards, and the additional information is of limited value in assessing risks. Regulatory requirements related to SFT reporting also must be rationalized and adjusted to ensure that they are not duplicative and meet the needs of regulators.

Proposed Solutions

Form N-PORT: The SEC should propose amendments to the Data Modernization final regulations to reallocate the information to be reported between existing forms and the new reporting form. Under the amendments, the Commission should reinstate Form N-Q and remove Part F from Form N-PORT to (together with Form N-CSR for fund annual and semi-annual shareholder reports) serve as the vehicle for providing investors and the public with quarterly information about fund portfolio holdings. Form N-PORT could then provide the Commission with substantially more detailed information in a structured format for regulatory oversight purposes, on a non-public basis for all months.

Additionally, the industry commenced extensive efforts to prepare for filing Form N-PORT immediately upon publication of the final rule. These efforts have demonstrated the enormity of the undertaking required to create the necessary infrastructure to support the new requirements. Much of the information, even if kept at some level in an organization, has to be newly sourced and compiled in standardized form, vetted for accuracy and technical compliance, and ultimately automated to ensure ability to comply with the new monthly filings. Further, the form requires extensive information that is not currently retained in the detail or specific data fields required by the form. Building the infrastructure requires the dedication of an unprecedented level of human and technical resources, and at a time when funds and advisers are responding to many and diverse new regulatory requirements. Accordingly, the SEC should delay implementation for at least eighteen months from the current implementation deadlines.

Form ADV: The SEC should also propose amendments to Form ADV to remove the new public reporting requirements related to separate account information, recognizing that the harms of public reporting outweigh any potential benefit. Additionally, the proposed amendments should seek to rationalize and adjust existing reporting requirements with other regulatory agencies to ensure the reports have standardized definitions and are not duplicative in nature.

With regard to the changes to Form ADV, the SEC should also immediately extend the compliance deadline by eighteen months, which would allow both the SEC and the industry

sufficient time to implement the new form. Given that the first delivery date is currently scheduled for six months from now and a test platform is not yet available, we have heard from many of our members that it will be difficult to meet the impending deadline. An eighteen-month delay would help ensure that the transition goes more smoothly.

3. Electronic Delivery of Regulatory Documents

As part of the proposal in which the SEC sought comment on these expansive new regulatory reporting burdens, the SEC also proposed a rule (Rule 30e-3) that would have reduced costs and burdens currently incurred by funds in connection with shareholder reports. Proposed Rule 30e-3 would have permitted electronic notification and web delivery of shareholder reports under conditions designed to preserve investor choice with respect to paper versus electronic delivery. Despite widespread industry support for proposed Rule 30e-3, the SEC dropped that part of the proposal in its final rule adoption, and declined to adopt it.

Need for Recalibration

Core Principles (a), (f), and (g)

Rule 30e-3 was an important part of the proposal, which has been abandoned mainly due to political pressures from the paper industry and others. Rules requiring paper communication are antiquated and inefficient, ignoring advances in technology and the evolution of consumer preferences, while wasting enormous amounts of paper and other resources and aggravating investors. We believe not only would this common-sense provision ensure that shareholder reports are distributed in the most efficient and effective manner possible, but also it would better empower Americans to make informed choices in the marketplace.[64]

Proposed Solutions

Treasury should recommend in the Report and in meetings with members of the FSOC that agencies require universal consent to electronic delivery or electronic access for all regulatory documents, rather than current requirements for consent on a per-agency, per document, per account basis. Additionally, Treasury should recommend Congress amend the Electronic Signatures in Global and National Commerce Act ("**ESIGN**"), which has not been updated since 2000, to broaden the scope of the legislation to address all regulatory document delivery, not just a limited subset of documents, and make consent to electronic delivery of documents less burdensome.

To the extent that legislation is infeasible, we would also urge the SEC to finalize Rule 30e-3 as soon as the Commission has a new Chairman, so that the cost savings can be passed on to the investors. Treasury should also ask the SEC to work together with the DOL to consider additional

[64] ICI estimated that default electronic access in lieu of delivery for mutual fund shareholder reports, would have resulted in industry-wide initial net cost savings of $89 million annually after the first year, and $140 million in net savings within the first three years of adoption. *See* Letter from David W. Blass, General Counsel, Investment Company Institute, to the U.S. Securities and Exchange Commission (Aug. 11, 2015), https://www.sec.gov/comments/s7-08-15/s70815-315.pdf.

rule changes that could be made to continue to lessen the administrative burden from regulatory consent documentation, given our evolving world and investor base.

4. Liquidity Risk Management

On October 13, 2016, the SEC adopted a new rule that will require mutual funds to adopt formal liquidity risk management programs, which must include certain prescribed elements mandated by the SEC in the rule.[65]

The prescribed elements include:

- A detailed liquidity classification system, which would require classification of each of the fund's portfolio investments (including derivatives) into one of four categories, based on the number of days reasonably expected to convert the investment to cash, or in some cases sell the investment, without the conversion to cash or sale significantly changing its market value, under current market conditions.

- Public reporting of portfolio liquidity, based on the prescribed classification system.

- Establishment of a "highly liquid investment minimum," or a policy setting the percentage of the fund's assets held in highly liquid investments.

- Continuation of the current "15% illiquid limit," which prohibits an open-end fund from acquiring illiquid investments once 15% of its assets are illiquid.

- Early warning reporting to Fund Boards and the SEC, both when the 15% illiquid limit is breached and for shortfalls in the highly liquid investment minimum.

Larger fund complexes must comply with the requirements by December 1, 2018, while smaller fund complexes will have until June 1, 2019 to comply.

The classification determinations under the final rule must take into account relevant market, trading, and investment-specific considerations, and must be based on information obtained after reasonable inquiry. While the SEC, to its credit, intended to provide a simplified classification process, relative to the classification categories and process that had been proposed and which were widely criticized as unworkable, in practice the final rule does not work as intended. One main element in the "simplified" classification process involves the express ability to classify assets by asset class, rather than on a holding by holding basis. However, the rule as adopted does not have the intended effect, due to a number of requirements added in the final version. First, the classification process must consider "market depth," which in itself is a complex analysis based on a number of factors. Second, the final rule imposes an "exception" process, under which the fund must separately classify and review (that is, not take advantage of asset mapping for) any investment if the fund or its adviser has information about any market, trading, or investment-specific considerations that are reasonably expected to significantly affect its liquidity characteristics as

[65] Investment Company Liquidity Risk Management Programs, 81 Fed. Reg. 82,142 (Nov. 18, 2016).

compared to other holdings within the asset class. Because of these and other complexities, and counter to the SEC's intent to simplify the rule, there is concern that actual implementation of the classification system will lead to managers having to monitor holdings daily, on an individual holding basis.

Need for Recalibration

Core Principles (a), (f), and (g)

The SEC's goal in adopting these requirements was to enhance liquidity risk management practices across the mutual fund industry, though the SEC acknowledged in its adopting release that most managers already employed liquidity risk management practices. Recognizing the significant burdens that would be imposed by the rule as originally proposed, and the absence of commensurate benefits, the SEC made changes in the final rule that were intended to make the rule simpler and more workable in practice. However, the final rule's adjustments did not have the intended simplifying effect, and the rule remains overly complex and burdensome. Most importantly, these burdens are unnecessary and will not provide appreciable benefits relative to current industry practices, existing SEC guidance, and the ability for (and current practice of) the SEC to ask about liquidity risk management practices in exams.

The open-end fund industry is highly diverse. Effective liquidity risk management across the open-end fund industry will best be achieved when all open-end funds have in place liquidity risk management programs that are developed and implemented based on sound principles in a manner that reflects and takes into account their specific circumstances. The Commission's rulemaking should be flexible enough to allow funds with effective liquidity risk management programs in place to continue to use and build on them, while requiring funds with less robust practices to develop and adopt programs that benefit from the experience and examples set by the industry leaders the Commission has observed.

If asset managers are required to categorize and report liquidity, particularly per fund and per position to the SEC and report aggregate percentages publicly, the additional operational complexity and costs of compliance will be exponential. These costs are not outweighed by any potential marginal benefit to the SEC, the capital markets, or investors. On the contrary, in light of the inherent subjectivity and fluid nature of liquidity determinations, the prescriptive classification system adopted in the final rule would likely produce data that conveys a false sense of precision and comparability across funds, rather than information that is meaningful for understanding or managing liquidity risk. Certainly the benefit of this information would not justify the massive initial and ongoing resources that funds will need to commit to implement the rule, even where they already have robust liquidity risk management systems already in place.

We fully support the SEC adopting a final rule that ensures that investment managers have liquidity risk management programs in place that take into account liquidity and manage it in the ordinary course. As part of these requirements, we also support early notifications to the SEC, should a problem arise, as well as codification of the current 15% illiquid limit. However, the formal classification system prescribed by the final rule should be abandoned, and the Board of Director requirements should be eliminated. To do otherwise mixes up roles and responsibilities of the

Board, which is focused on oversight, and the investment manager, which is focused on the day-to-day portfolio management. It also unnecessarily constricts the investment manager and fund, potentially adding more risk – and definitely more cost – unnecessarily to the system.

At a minimum, the SEC should delay the current implementation date to allow the industry additional time to calibrate its systems and to determine whether vendors can reasonably be expected to develop solutions that will help meet the onerous rule requirements (to date such viable vendor solutions have not been demonstrated), and to create enough time to provide the industry with guidance as to how to address some of the more complex and unworkable parts of the final rules. Each one of our members is spending significant time and resources working through this complex rulemaking, and the list of operational issues seems to grow daily. These concerns include how to address the adviser/subadvisor relationship, and to what extent an adviser can rely upon its subadvisors to do the classifications (and, relatedly, what should be done if subadvisors have conflicting classifications). The absence of viable vendor solutions to meet the needs of asset managers under this rule, and the difficulties asset managers are experiencing building out appropriate systems to address unexpected operational complexities embedded in the rule, both argue strongly for a delayed compliance date. Additional time would also be helpful at getting Boards up to speed on their new requirements, given already scheduled Board meeting dates.

Proposed Solutions

The final rule does not promote the Core Principles and we urge Treasury to recommend that the SEC immediately delay this rulemaking at least eighteen months from the implementation deadlines under the final rule and use this delay period to consider the unintended consequences that are manifesting themselves, which defeat the intended "workability" of the rule.

After analyzing the operational concerns that have become apparent to the industry, we would urge the Commission to propose a rulemaking to address these issues. Broadly speaking, the proposed rulemaking should abandon the prescriptive components of the current regulations, and instead require asset managers to adopt a principles-based liquidity risk management program, thus raising the bar across the industry. The new rulemaking should completely eliminate the onerous and harmful liquidity classification system and instead focus on principles that should be considered in each liquidity risk management program. It should, however, retain the most important parts of the current rulemaking, including codifying the 15% illiquid restriction as well as requiring early warning reports to the SEC, should problems arise.

5. Business Continuity Planning and Transition Plans

On June 28, 2016, the SEC proposed (but has not finalized) a rulemaking that would require registered investment advisers to adopt and implement written business continuity and transition plans. According to the SEC, the proposed rule is designed to ensure that investment advisers have plans in place to address operational and other risks related to a significant disruption in the adviser's operations in order to minimize client and investor harm.

AMG supported the SEC's objective – to mitigate the risks of business disruptions for investors – because our members have historically prioritized the implementation of comprehensive

and robust principles-based business continuity programs. However, we have significant concerns with the SEC's actual rule proposal. In particular, we strongly urged the SEC to avoid imposing "fraudulent" liability for business continuity practices and establishing a new, unprecedented level of accountability for functions carried out by third-party service providers. Additionally, the AMG argued that separate transition planning requirements for advisers are unnecessary since current operational management practices and the existing regulatory framework already addresses any transition-related concerns cited by the SEC that may impact investors. AMG also urged the SEC to ensure that any resulting obligations for registered investment advisers align with the approach already established for broker-dealers and other market participants by the SEC, the FINRA, the CFTC, and others.

Need for Recalibration

Core Principles (f) and (g)

Given that the obligation to engage in responsible business continuity planning is not a new consideration for registered investment advisers, and that thousands of funds and dozens of advisers enter and exit the market every year with no discernible impact,[66] AMG firmly believes that this rulemaking was again drafted in order to stave off macroprudential regulation. There is no need to create a new special resolution or business continuity/transition planning regime to facilitate these closures. They are part of the normal business cycle, and on multiple occasions over the years, the SEC has set forth expectations around business continuity that are appropriate for individual firms and the position occupied by asset managers in the larger financial intermediary space.[67] Existing measures are effective – there is no need for a bank-style living will requirement.

The SEC has also noted when adopting regulations in this area for other market participants, that advisers generally pose less risk to the financial markets than other regulated entities.[68] Specifically, the SEC indicated when adopting Regulation Systems Compliance and Integrity ("**Reg SCI**") that advisers were not among the types of entities that have "the potential to pose the most significant risk in the event of a systems issue" – suggesting that registered investment advisers do not pose the same potential risks to market stability as other market participants, such as SCI entities, when faced with significant disruption events and therefore, that existing regulations are sufficient.[69]

Despite this history and without any examples of situations where the existing regime was inadequate, the SEC drafted a rulemaking with a prescriptive, untailored framework, that effectively imposes strict liability on advisers for disruptions of any kind, which will inherently interfere with

[66] *See. e.g.,* Simone Foxman, *More Hedge Funds Shut Last Year Than Any Time Since the 2008 Crisis*, Bloomberg, (Mar. 17, 2017), https://www.bloomberg.com/news/articles/2017-03-17/more-hedge-funds-shut-last-year-than-any-time-since-2008-crisis.

[67] *See* Letter from SIFMA AMG to the SEC on Business Continuity Planning, Transition Plans and Related Recordkeeping (Sept. 1, 2016), http://www.sifma.org/issues/item.aspx?id=8589962057.

[68] *Id.*

[69] *Id.*

well-established industry best practices that enable an adviser to rely on the expertise of the business continuity professionals to lead them through emergent situations.

Additionally, again taking a page out of the bank regulator's playbook, the SEC included transition planning requirements in the rulemaking. Transition plans are an inappropriate risk mitigation tool for investment advisors, because advisers and funds "routinely transition client accounts without a significant impact to themselves, their clients, or the financial markets."[70] This smooth transitioning results from the expectations set by existing regulations and market discipline. Further, as a practical matter, since advisers operate in an agency capacity and do not directly absorb investor losses, they are highly unlikely to become insolvent suddenly and unexpectedly or to experience unexpected financial distress.

Proposed Solutions

The SEC should abandon the proposed rule and instead issue guidance on business continuity planning that builds upon its successful approach to business continuity planning under Rule 206(4)-7 under the Advisers Act, issuing guidance for public comment that appropriately address any concerns while remaining within the limitations of the Advisers Act. Should the SEC determine that a new rule is necessary, it should be re-proposed, focusing solely on business continuity planning, removing the "fraudulent" liability for business continuity practices and removing any requirements for "transition planning."

6. Leverage and the Use of Derivatives Rulemaking

On December 28, 2015, the SEC proposed a rulemaking to regulate the use of derivatives by registered investment companies and business development companies (collectively, "**Regulated Funds**") by establishing limits on the size of derivatives and other senior security positions, codifying and adjusting asset segregation requirements, and requiring regulated funds having large positions in derivatives to establish risk management programs.[71]

The main components of the proposal are: (1) Portfolio limits – The proposal would impose portfolio construction restrictions that would, for the first time, put an outer limit on the amount of a fund's use of derivatives; (2) Asset segregation – The proposal would consolidate and rationalize the current "patchwork" of staff positions on the amount and nature of assets funds must set aside as "cover" for their derivatives exposure; and (3) Risk management – Funds with derivatives usage above a certain level would be required to adopt and implement a Board-approved derivatives risk management program with certain specified elements.

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[70] *Id.*

[71] *See* Use of Derivatives by Registered Investment Companies and Business Development Companies, 80 Fed. Reg. 80,883 (Dec. 28, 2015).

Need for Recalibration

Core Principles (a), (f), and (g)

AMG supports the SEC's objectives of enhancing open-end fund practices for derivatives risk management and consolidating and updating its guidance regarding the use of derivatives by regulated funds. However, given that derivatives are important portfolio management tools, both for hedging and investing, the SEC's proposed limitation on the use of derivatives are neither necessary nor appropriate. The SEC's policy objectives would be better addressed through codifying and improving asset segregation requirements.

Proposed Solutions

The SEC should withdraw its proposal on setting leverage limits, and not move forward with setting limits on the use of derivatives by Regulated Funds unless limits are supported by the enhanced data that it will be receiving through its rule changes on investment adviser and fund reporting. The SEC's data collection rule, once implemented, will yield at least some information on a fund's leverage, which could be informative to understanding current leverage levels and whether any issue is present under the current rules, which already require asset segregation to cover liabilities. While we believe this data will support the conclusion that limits should not proceed, certainly, the SEC should not move forward with limits until it has the benefit of this analysis.

The SEC, however, should codify the requirements for asset segregation, which presently are determined by interpreting a series of staff guidance (Investment Company Act Release 10666, issued in 1979, followed by more than 30 no-action letters) (the "Asset Segregation Requirements") and correct, clarify, and modernize the Asset Segregation Requirements. In codifying the requirements, the SEC should correct or clarify known issues with the Asset Segregation Requirements and harmonize requirements with existing standards imposed by other regulations.

C. CFTC Regulation of Funds and Advisers

Following adoption of Dodd-Frank, the CFTC has amended its regulations and taken positions that effectively create a dual regulation regime for many SEC registrants. These actions imposed widespread, duplicative, and sometimes inconsistent, CFTC regulation on SEC registered funds and advisers, which are already subject to comprehensive regulation by the SEC, their primary regulator. This dual regulation has dramatically multiplied the regulatory burdens on SEC-registered funds and advisers, without providing a commensurate benefit to the markets or to investors, and in fact has increased investor costs while reducing investor choice.

In addition, the CFTC has signaled a "zero tolerance" approach to U.S. investment in offshore commodity pools. Under this approach, a single U.S. investor in an otherwise entirely offshore fund, even if unknown or inadvertent, could place the fund and its adviser within the reach of the CFTC's registration requirements.

Compounding the impact of these actions, in interpreting and implementing its new regulatory authority under Dodd-Frank, the CFTC has applied a "one swap" test to its jurisdiction

over commodity pool operators and commodity trading advisors.[72] This policy combined with the international nature of the swaps market has resulted in an even broader and extraterritorial expansion of the CFTC's fund and adviser regulation remit, overlapping in many instances with regulations applicable to funds and advisers in other jurisdictions.

Overly broad and dual regulation represents the very converse of regulation that is efficient, effective, and appropriately tailored. Duplicative and inconsistent regulation impedes rather than fosters economic growth and vibrant financial markets by, among other consequences, stifling competition and innovation. Assertion of U.S. registration requirements on essentially offshore activities, where the interests of U.S. investors are at best *de minimis*, conflicts with basic principles of international comity and the goal of enhancing the competitive position of U.S. companies.

These actions have amounted to either a significant reversal of prior CFTC interpretations or policy positions, or an open disregard for explicit statutory language and precedent, and all were taken without evidence of harm to investors or the markets justifying the change. None of them was required by Dodd Frank, or tied to the financial crisis. Thus, eliminating these recent actions would restore the regulatory regime for SEC-registered funds and advisers to a balance of regulatory authority which was developed over the course of nearly 75 years, and which has well served both investors and the markets.

Need for Recalibration

Core Principles (f)

The CFTC 2012 amendments of CFTC Rule 4.5.[73] In 2012, the CFTC amended Rule 4.5, which since 2003 had provided an exclusion from commodity pool operator ("**CPO**") regulation for funds registered under the 40 Act and their advisers. The amendments imposed two tests for a 40 Act fund to claim the exclusion from CPO registration: a commodity interest *de minimis* trading test and a marketing test. If the 40 Act fund fails either test, the fund's adviser has to register with the CFTC as a CPO and become a member of the National Futures Association ("**NFA**").

As a result, amended Rule 4.5 now requires all registered funds to analyze, and monitor on an ongoing basis, whether they meet both of the tests for the CPO exclusion, many of the terms of which are ambiguous and subjective. This in itself is a burdensome, costly, and labor intensive process.

Moreover, advisers to funds that do not meet both tests are required to register as CPOs. While the CFTC provided so-called "harmonization" exemptions for some of the requirements otherwise applicable to CPOs, which permit 40 Act fund CPOs to rely on substituted SEC compliance for most CFTC disclosure and shareholder reporting requirements, many significant areas of CPO regulation are not harmonized for 40 Act fund CPOs, including, among others, the following:

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[72] *See, e.g.*, Commodity Pool Operators and Commodity Trading Advisors: Compliance Obligations, 77 Fed. Reg. 11252 (Feb. 24, 2012) ("one swap contract would be enough to trigger the registration requirement.").

[73] CFTC Regulations are found by their section under Title 17 of the Code of Federal Regulations.

Record keeping. SEC-registered advisers that are now required to register with the CFTC as CPOs are subject to the full set of CFTC record keeping requirements. Notwithstanding that these SEC registrants already comply with the SEC's comprehensive record keeping requirements, they must also consult and comply with an entirely separate set of record keeping rules. While the purposes overlap, there are, naturally, some differences, which creates an entirely unnecessary duplication of effort.

Regulatory reporting. SEC-registered adviser CPOs also must comply with the CFTC's and NFA's complex and burdensome regulatory reporting regime, including quarterly or annual filing for CFTC Form CPO-PQR (depending on the size of the adviser) and quarterly filing of NFA Form PQR. These forms, while designed to serve the same regulatory oversight goal sought by the SEC in its reporting forms, require different formats and reporting styles, resulting in labor intensive dual reporting.[74]

NFA rules. SEC-registered adviser CPOs must comply with an additional comprehensive set of NFA rules and filing requirements. These add yet another regulatory overlay, in this case with variations designed historically for an entirely different set of markets and market participants.

Importantly, the CFTC's actions in significantly narrowing the CPO exclusion for registered funds reflected an abrupt reversal of its decision in 2003 to expand the exemption. The CFTC's reasoning in 2003, which effectively took SEC-registered funds out of the CFTC's CPO registration requirements, was as follows:

> [The expanded exclusion] is intended to allow greater flexibility and innovation, and to take into account market developments and the current investment environment, by modernizing the requirements for determining who should be excluded from the CPO definition, and who should remain within the CPO and CTA definitions but be exempt from registration. Thus, this relief is intended to encourage and facilitate participation in the commodity interest markets by additional collective investment vehicles and their advisers, with the added benefit to all market participants of increased liquidity.[75]

In its 2012 determination to once again narrow the exclusion for SEC-registered funds, and indeed further restrict it, the CFTC did not explain how the original goals cited above – allowing greater flexibility and innovation and providing all market participants the benefit of increased liquidity –would continue to be served. We believe the 2012 actions have in fact greatly impeded these goals, and that returning to the expanded exclusion would once again foster the flexibility,

[74] The burdens of duplicative reporting are now being compounded as 40 Act Funds and their adviser prepare for compliance with the SEC's new modernized reporting requirements, which will substantially expand the amount and frequency of data that funds and advisers must report. *See* Investment Company Reporting Modernization, 81 Fed. Reg. 81870 (Nov. 18, 2016); Form ADV and Investment Advisers Act Rules, 81 Fed. Reg. 60418 (Sept. 1, 2016).

[75] *See* Additional Registration and Other Regulatory Relief for Commodity Pool Operators and Commodity Trading Advisors; Past Performance Issues, 68 Fed. Reg. 47221, at 47223 (Aug. 8, 2003), citing the reasons for the proposal as explained in the proposing release, 68 Fed. Reg. 12622 (March 3, 2003).

innovation, and market liquidity that the CFTC has historically seen as beneficial to investors and the markets.

CFTC's revocation of Rule 4.13(a)(4). Also in 2012, the CFTC repealed Rule 4.13(a)(4), which had provided an exemption from CPO registration for operators of private funds relying on the SECs' private offering exemption, where pool participants met certain specified sophistication criteria. Following this revocation, operators of these funds have either had to rely on a different exemption, which, like amended Rule 4.5, imposed both a commodity interest trading test and a marketing test, or register as CPOs and become NFA members. There are no harmonization exemptions for private fund CPOs that are SEC-registered advisers, although another CFTC rule permits streamlined compliance for CPOs of funds that are sold only to certain sophisticated or institutional investors.

CFTC's policy on "one swap" and inadvertent commodity pools. A combination of parallel developments in 2012 also dramatically magnified the impact of the CFTC's cut back of the CPO exemptions, by expanding the number of funds that were considered commodity pools. First, swaps became commodity interests under Dodd-Frank, starting with the effective date of the CFTC's rules implementing the new definitions. Second, the CFTC took the position that every pooled vehicle holding even a single swap (including non-deliverable currency forwards) is presumptively a commodity pool. Finally, these developments were compounded by the CFTC's position that a fund investing in a commodity pool is itself a commodity pool.

We do not take issue here with the expanded definition of commodity interest, which following the financial crisis Congress determined should include swaps. However, we believe that the staff's broad interpretation of the term commodity pool to include, presumptively, any pooled vehicle holding even a single swap, for any reason, is at odds both with the statutory definition and any reasonable regulatory policy.

With respect to the statutory definition, Section 1a(10) of the Commodity Exchange Act ("**CEA**") defines the term commodity pool to mean "any investment trust, syndicate, or similar form of enterprise **operated for the purpose of trading in commodity interests**..." (emphasis added). Many vehicles, including securitization vehicles and other vehicles that use swaps or futures simply for hedging outstanding debt, cannot by any common sense understanding of the words be viewed as "operated for the purpose of trading in commodity interests." The same is true for funds with exposure to emerging markets that use currency forwards only for hedging that exposure back to U.S. dollars. Yet the staff has repeatedly refused to adopt a plain English understanding of the words, and appears to consider any vehicle holding a single swap to be a commodity pool, absent specific CFTC or staff authority to the contrary. This labor intensive regulatory approach - every pool holding a swap is "in" until the staff says it can be considered "out -- creates a regulatory bottleneck that not only stifles and raises the cost of innovation, but also puts an enormous strain on CFTC resources that could more effectively be used elsewhere.

Moreover, combined with the CFTC's position that a fund holding one of these "inadvertent commodity pools" is itself a commodity pool, the "one swap" approach would require every fund that invests in those vehicles to determine if they are covered by a staff no-action letter, or otherwise to "look through" the vehicle to determine whether the fund meets the trading test on

an indirect basis. This creates an unmanageable level of complexity in connection with monitoring for compliance with the Rule 4.5 trading restrictions.

The CFTC's zero tolerance for U.S. investment in offshore funds (the "single U.S. investor" interpretation). The CFTC has expressed the view that under the CFTC's rule providing an exemption for offshore operators of offshore funds (Rule 3.10(c)(3)) on behalf of non-U.S. investors, the operator of a non-U.S. fund with even one U.S.-based owner is required to register as a commodity pool operator.[76] This approach, which provides no comfort for funds that do not solicit or market in the U.S. or to U.S. investors, and even explicitly prohibit U.S. persons from investing, is inconsistent with general principles of international comity, as well as the CFTC's own statements of policy on appropriate use of its resources:

> [G]iven this agency's limited resources, it is appropriate at this time to focus the [CFTC's] customer protection activities upon domestic firms and upon firms soliciting or accepting orders from domestic users of the futures markets and that the protection of foreign customers of firms confining their activities to areas outside this country, its territories, and possessions may best be for local authorities in such areas.[77]

Additionally, since 10% tolerance for US investors in ex-US products already exists in other CFTC regulations, the CFTC would not be establishing a precedent in granting the same under Rule 3.10(c)(3).

Proposed Solutions

In order to improve the efficiency of fund and adviser regulation and avoid redundancies that do not advance regulatory needs, we recommend that the CFTC:

- Reverse its 2012 amendments of CFTC Rule 4.5;
- Reverse its revocation of CFTC Rule 4.13(a)(4); and
- Revise its policy on "one swap" and inadvertent commodity pools.

Should the CFTC not zero out the registration overlap of SEC-registered funds and advisers, it should make further improvements to substituted compliance requirements for those dually registered entities.

D. CFTC Regulation of Derivatives Markets

1. Position Limits

For many years, the CFTC has weighed whether and at what level to expand position limits for futures contracts and certain off-exchange contracts viewed as economically equivalent. The

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[76] *See* Interpretive Guidance and Policy Statement Regarding Compliance with Certain Swap Regulations, 78 Fed. Reg. 45292 n. 149 (July 26, 2013) ("Under Commission regulation 3.10, the operator of a non-U.S. fund with even one U.S.-based owner is required to register as a commodity pool operator.").

[77] *See* Exemption from Registration for Certain Foreign Persons, 72 Fed. Reg. 63976 (Nov. 14, 2007), citing 48 Fed. Red. 35461 (Aug. 3, 1983).

complexity of the task is illustrated by the series of rulemaking notices, withdrawals, and re-proposals that have preceded this re-proposed position limits rulemaking. The first rulemaking notice that the Commission issued was subsequently withdrawn.[78] The CFTC issued a second notice, and adopted rules in 2011,[79] but ultimately the D.C. District Court vacated the rules because the court found that section 4a(a)(1) of the Act "clearly and unambiguously requires the CFTC to make a finding of necessity prior to imposing position limits".[80] In 2013, the CFTC issued a third notice, relating to aggregation of positions, and a fourth notice, relating to reproposed position limits.[81] The CFTC then issued a revised reproposal pertaining to aggregation of positions and federal position limits,[82] and adopted final rules on aggregation of positions.[83]

Asset managers have a keen interest in whether federal position limits are established and, if so, the process by which those positions are set. Asset managers utilize commodity derivatives in their capacity as fiduciaries to private and public funds as well as separately managed accounts for a wide range of investors and retirement savers, and rely on fair, competitive and transparent pricing and liquidity. Investment funds and separately managed account clients play a vital role in these markets by assuming price risk from commercial participants (hedgers) on the long and short sides of the market, and providing the liquidity that facilitates price discovery and risk transfer for businesses around the world.

Need for Recalibration

Core Principles (f)

AMG believes that position limits for futures contracts should not be imposed by the CFTC but rather should be left to futures exchanges, and should not extend to off-exchange contracts.

AMG is concerned that any rule that would prevent asset managers from trading on behalf of their clients or unnecessarily or disproportionately increase the costs of compliance would harm the liquidity and price discovery function of the derivatives market. Specifically, AMG continues to have serious concerns with the CFTC's proposed position limits framework, including its fundamental underpinnings. Without having made a finding that excessive speculation exists in the markets or that position limits are necessary in each of the core referenced futures contracts, we believe that the CFTC's economic basis for justifying its regulatory policy and methodology for

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[78] Federal Speculative Position Limits for Referenced Energy Contracts and Associated Regulations, 75 Fed. Reg. 4,144 (proposed Jan. 26, 2010), *withdrawn* 75 Fed. Reg. 50,950 (Aug. 18, 2010).

[79] Position Limits for Derivatives, 76 Fed. Reg. 4,752 (proposed Jan. 26, 2011); Position Limits for Futures and Swaps, 76 Fed. Reg. 71,626 (adopted Nov. 18, 2011); vacated by *Int'l Swaps & Derivatives Ass'n v. U.S. Commodity Futures Trading Comm'n*, 887 F. Supp. 2d 259 (D.D.C. 2012).

[80] *Int'l Swaps & Derivatives Ass'n*, 887 F. Supp. 2d at 269.

[81] Aggregation of Positions, 78 Fed. Reg. 68,946 (proposed Nov. 15, 2013); Position Limits for Derivatives, 78 Fed. Reg. 75,680 (proposed Dec. 12, 2013).

[82] Position Limits for Derivatives and Aggregation of Positions, 80 Fed. Reg. 10,022 (proposed Feb. 25, 2015).

[83] Aggregation of Positions, 81 Fed. Reg. 91,454 (Dec. 16, 2016).

implementing position limits remains flawed. AMG believes that regulatory policy, especially a policy as significant and with such a profound market impact as position limits, should be designed based on sound market and economic principles. Instead, the CFTC's proposals use a simplistic one-size-fits-all approach to establish position limit levels based on a generic percentage of deliverable supply and open interest.

AMG also has concerns with the CFTC's final aggregation rule, which establishes the standards by which certain interests should be combined for determining the total position to be judged against a position limit in the futures contract.[84] The aggregation rule imposes burdensome disaggregation notice filings, aggregates positions on the basis of an unworkable "substantially identical trading strategies" standard, and unnecessarily limits disaggregation for certain accounts controlled independently.

Proposed Solutions

AMG recommends that the CFTC not proceed with additional federal position limits. If the CFTC determines to move forward with position limits, AMG requests that the CFTC narrowly tailor the framework to achieve a specific market outcome, in a way that is designed to be minimally disruptive, practical, and not overly complicated to administer by market participants. The CFTC should examine carefully all relevant data and consider available alternatives in determining whether there are demonstrable concerns over excessive speculation. Specifically, the CFTC should identify a clear standard of "excessive speculation" and incorporate that standard in its required necessity findings. In addition, before imposing position limits on a core referenced futures contract,[85] make a necessity finding specific to such core referenced futures contract and explain why position limits, and the levels at which they are fixed, are appropriate for each such contract. These steps should be supported by empirical evidence of the need for the position limits and the levels at which position limits are established, including substantive economic, data-based rationale.

To the extent the CFTC makes a necessity finding and determines that position limits are appropriate for a specific core referenced futures contract, AMG would recommend a number of considerations that AMG recently made to the CFTC in its comment letter filed on February 28, 2017.[86]

For the CFTC's final aggregation rule relating to position limits, AMG recommends removing the notice filing requirements for disaggregation, removing the aggregation standard for "substantially identical trading strategies," and expanding the independent account controller aggregation exemption to apply to exempt commodity trading advisers.

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[84] *Id.*

[85] In the Reproposal, the CFTC defines "core referenced futures contract" to mean "a futures contract that is listed in § 150.2(d)." The table in Proposed Rule 150.2(d) identifies 25 contracts as core referenced futures contracts.

[86] See SIFMA AMG and Other Associations Submit Comments to the CFTC on Position Limits for Derivatives (Feb. 28, 2017), http://www.sifma.org/issues/item.aspx?id=8589965403.

2. Regulation Automated Trading

The CFTC proposed Reg AT in 2015 and reproposed the rule in 2016. Reg AT broadly seeks to address algorithmic commodities trading by requiring the registration of entities engaged in algorithmic trading using direct electronic access to a designated contract market overseen by the CFTC; and standardizing pre-trade risk controls and adopting trade reporting and other transparency measures, as well as other safeguards to protect market participants.

Reg AT mandates overlapping, redundant risk controls at multiple levels, proposing to impose responsibilities on algorithmic traders and other commodity trading principals using direct electronic access to DCMs, requiring many of them to become registered with the CFTC as "AT Persons," FCMs, and designated contract markets. Reg AT leverages certain existing registration categories that are unrelated to algorithmic trading, leading to application to asset managers that are unclear and unduly burdens registered funds and advisers. In addition, for asset managers that often use algorithms provided by FCMs, Reg AT results in adding burdens that do not advance the safety of designated contract markets.

Need for Recalibration

Core Principles (f)

AMG believes that the Reg AT unnecessarily burdens designated contract markets. While AMG supports the CFTC's aim of protecting futures exchanges and market participants from the potential risk of market disruption that could be caused by a lack of controls on certain types of algorithmic trading, AMG does not support the unnecessarily complex, overbroad, redundant, burdensome, and costly framework that would be imposed by the Proposed Reg AT proposal, as originally formulated in the CFTC's 2015 proposal and as modified in the supplemental proposal released in late 2016.

Proposed Reg AT is very complex, and it would impose new and costly burdens on market participants, as well as on the CFTC. As noted in our prior comment letter, the futures industry currently adheres to and benefits from an existing best practice and regulatory framework applicable to algorithmic trading implemented by designated contract markets that largely addresses the goals of Proposed Reg AT.[87] The CFTC has authority to oversee DCMs and could easily exercise such authority to monitor existing DCM risk controls over algorithmic trading. Proposed Reg AT would impose on market participants additional unnecessary, redundant, burdensome and costly layers of regulatory oversight. Proposed Reg AT's costs will far exceed any incremental benefits the CFTC's proposed redundant framework may provide that are not already being achieved by DCMs. This is a good example of where the CFTC, which has limited financial and personnel resources, could wisely utilize the resources and expertise of other self-regulatory organizations (such as designated contract markets) in administering regulatory goals and to "regulate smarter."

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[87] See SIFMA AMG Letter to the CFTC on proposed Regulation Automated Trading (Mar. 16, 2016), http://www.sifma.org/issues/item.aspx?id=8589959344.

Proposed Solutions

Proposed Reg AT should not be adopted. Instead, the CFTC should continue to rely on designated contract markets to manage stability risks, which the CFTC can assess through its oversight of designated contract markets. If the CFTC moves forward with regulation in this area, AMG recommends that the CFTC focus on non-redundant risk controls as opposed to additional registration categories and access to highly confidential source code.

3. Central Execution of Swaps on Swaps Execution Facilities

The CFTC has taken significant steps previously towards implementing the G20 commitment to, where appropriate, require central execution of standardized, liquid OTC derivative contracts; however, as stated in prior letters to the CFTC and at roundtables, AMG members believe that changes to Part 37 of the CFTC's Regulations and certain designated contract market rules are required to make central execution of swaps work efficiently for the market and market participants. At the same time, certain protections and structural fairness must be maintained and strengthened given the that swaps mandated for central execution must be execution on a swap execution facility ("**SEFs**").

Need for Recalibration

Core Principles (f)

As the CFTC has acknowledged through public statements (including many recommendations made by the Acting Chairman in his 2015 whitepaper, *Pro-Reform Reconsideration of the CFTC Swaps Trading Rules: Return to Dodd-Frank*[88]), roundtables and no-action relief, recalibration is needed for SEF trading.

Proposed Solutions

AMG believes that the CFTC should expand permitted modes of execution for swaps required to be traded on SEFs in order to provide for a less prescriptive, more principles-based approach that balances transparency, competition, and liquidity through a flexible set of rules. While we do not believe that any and every mode should be available, we believe that any means of execution that provides pre-trade price transparency should be permitted.

AMG believes that the CFTC should also fix known and identified problems with the Made Available to Trade ("**MAT**") process.[89] AMG believes that the MAT standards must be different from the clearing standards because, even with broader methodologies of execution, additional elements must be present for a swap to trade on a SEF. We believe that all six MAT factors

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[88] *See* J. Christopher Giancarlo, Commissioner, *Pro-Reform Consideration of the CFTC Swaps Trading Rules: Return to Dodd-Frank* (Jan. 29, 2015), http://www.cftc.gov/idc/groups/public/@newsroom/documents/file/sefwhitepaper012915.pdf.

[89] *See* SIFMA AMG Letter to the CFTC on Made Available to Trade Determinations (Aug. 17, 2015), http://www.sifma.org/issues/item.aspx?id=8589956080.

provided under CFTC Regulation 37.10 plus a number of additional factors (referenced below and detailed in AMG's 2015 letter[90]), should be met for a swap to be mandated for central execution. The CFTC should also address the problems raised relating to "package transactions" (also discussed in AMG's 2015 letter) such that only liquid and standardized package transactions capable of being traded on SEFs are mandated for central execution.

In addition, AMG believes that designated contract market rules should be changed to allow exchange of contracts traded on SEFs and designated contract markets without giving some venues the ability to restrict markets. Specifically, CME Rule 538 and ICE Rule 4.06 should be changed to allow swaps traded on SEFs to be exchanged for futures.

While AMG recommends these adjustments, AMG believes that impartial access should remain an important component of SEFs. SEFs should continue to establish objective eligibility criteria for any market participant to satisfy in order to become a member and gain access to their markets, without discriminating or relying on historical precedent. To do otherwise would unfairly prejudice market participants excluded from certain SEFs notwithstanding the mandate to trade on central platforms.

E. DOL Fiduciary Rule

In April 2016, the DOL finalized changes to the term "fiduciary" under section 3(21) of the Employee Retirement Income Security Act of 1974, as amended ("**ERISA**") and section 4975(e) of the Internal Revenue Code of 1986, as amended (the "**Code**"). At the same time, the DOL finalized revisions to related exemptions, including the Best Interest Contract Exemption (the "**BIC Exemption**").[91]

These revisions, which we collectively refer to as the DOL Fiduciary Rule, amount to a massive expansion of fiduciary obligations and, at the same time, a significant reduction of permissible conduct for ERISA fiduciaries. The DOL Fiduciary Rule affects every aspect of retirement investment services, from creation of products to relationships with individual investors. At the same time, certain exemptions within which ERISA fiduciaries must operate have been narrowed, repealed or tied to onerous restrictions on compensation and increased litigation risks.

While asset managers are already fiduciaries when they act as discretionary investment managers or provide investment advice to clients and largely are not directly impacted by the changes imposed by the DOL Fiduciary Rule, the secondary impacts of the rule upon asset managers' creation of investment products and the restrictions that asset managers need to impose on their own activities will result in a significant reduction of available choices and services for retirement savers.

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[90] *See* SIFMA AMG Letter to the SEC on the Division of Market Oversight's Public Roundtable Regarding the Made Available to Trade; Request for Further Relief from Trade Execution Requirements for Package Transactions (Aug. 17, 2015), http://www.sifma.org/comment-letters/2015/sifma-amg-submits-comments-to-the-cftc-on-made-available-to-trade-determinations/.

[91] 81 Fed. Reg. 20946- 21221 (Apr. 8, 2016).

Need for Recalibration

Core Principles (a) and (f)

The DOL Fiduciary Rule has already harmed investors as the market prepares for the upcoming implementation date and is likely to continue to harm investors by reducing retirement savers' access to retirement savings offerings, product structures, savings information, and related financial advice. AMG believes that the rule as a whole will result in asset managers being more restricted in making available services and/or products that are intended to facilitate wise investing at a reasonable cost and improve retirement investment outcomes.

AMG continues to strongly believe that national retirement policy should not be guided directly or indirectly by any one regulator's judgment as to which products and services may be in the best interest of any given retirement investor or plan. Nonetheless, the DOL Fiduciary Rule has had and, absent recalibration, will continue to have the effect of promoting certain types of products (*e.g.*, low-cost index products) over others. Asset managers, as manufacturers of the products sold by broker-dealers, can already see that the cost of certain products and services has been reconfigured and many providers have already culled the products and services available.

Business models and product offerings are being reconfigured with a strong nod to fear of litigation—rather than what is truly best in the Plan investor's interest. This fear has had the effect of stifling development of truly innovative retirement products and strategies.

The impact of potential future litigation is particularly troubling for the negative consequences upon American investors. As FINRA's chairman and chief executive officer observed, "i[n] one sweeping step, [the Fiduciary Rule] moves enforcement of these provisions to civil class action lawsuits. or arbitrations where the legal focus must be on a contractual interpretation."[92] The BIC Exemption, including its prohibition of contractual limitations on class action litigation, was designed to instill fear of litigation in firms who advise and serve investors. Firms will face the likelihood of facing numerous opportunistic litigations notwithstanding their efforts to act in a retirement investors' and plans' best interest. And the sheer expansion of fiduciary status, with its absence of mutuality, and its exceptions like "general communications," leave significant questions about their ultimate scope. Firms will either accept this uncertainty to their likely detriment or avoid these risks by severely restricting products and services. The frontiers between advice on the one hand and sales or education on the other hand remain fraught with the very type of ambiguity plaintiffs' lawyers love to explore.

In AMG's view, the rule negates instead of enhances an individuals' ability to save for retirement and build the individual wealth necessary to afford typical lifetime expenses, such as buying a home and paying for college, and to withstand unexpected financial emergencies.

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[92] Richard Ketchum, Remarks from the 2015 FINRA Annual Conference, available at https://www.finra.org/newsroom/speeches/052715-remarks-2015-finra-annual-conference.

Proposed Solutions

The DOL should defer application of the DOL Fiduciary Rule until completion of the review directed by the President's February 3, 2017 Executive Order.[93] During the delay period, the SEC and FINRA should continue their efforts to establish a uniform best interest standard for broker-dealers providing personalized advice.

AMG supports a "best interest" standard for financial professionals that would apply across all personalized investment advice made to retail investors. This result can be accomplished by establishing a uniform best interest legal standard promulgated by the SEC or FINRA for broker-dealers that applies to all retail brokerage accounts, not just accounts subject to ERISA and section 4975(e) of the Code. A uniform standard for personalized investment advice to retail investors could be imposed without the overly broad definition of investment advice, unnecessary subjectivity, and overlapping and expensive requirements currently contained in the DOL Fiduciary Rule, and particularly the BIC exemption. Indeed, the current Acting Chair of the SEC expressed support for delaying implementation of the DOL Fiduciary Rule so that the SEC could take a leading role under the new administration.[94]

F. Volcker Rule

Final Volcker Rule regulations were released and adopted by the agencies on December 10, 2013. The rules generally prohibit banking entities from:

- engaging in short-term proprietary trading of securities, derivatives, commodity futures and options on these instruments for their own account, and
- owning, sponsoring, or having certain relationships with hedge funds or private equity funds that are "covered funds" (as defined under the rules).
    - With respect to our bank-affiliated asset manager members, an exemption from Volcker Rule covered fund provisions permits them to organize and offer covered funds subject to various requirements, including:
        - The banking entity owning no more than 3% of the covered fund;
        - An overall limit of 3% of the banking entity's tier 1 capital invested in covered funds; and
        - A restriction on the banking entity sharing a name or a variant of the same name with the covered fund, among other limitations

Subject to certain limitations, banking entities may provide a covered fund with 100% of its initial equity "to permit the fund to attract unaffiliated investors," provided that the bank reduces its ownership to no more than 3% of the total ownership interests in the covered fund, through

[93] Presidential Memorandum on the Fiduciary Duty Rule (Feb. 3, 2017), https://www.whitehouse.gov/the-press-office/2017/02/03/presidential-memorandum-fiduciary-duty-rule.

[94] Michael Piwowar, Acting Chair, SEC, Remarks at the 2017 Policy Conference of the Mutual Fund Directors Forum (Apr. 21, 2017), as reported in Financial Advisor IQ, http://financialadvisoriq.com/c/1619083/186883.

redemption, sale, or dilution (or other methods) within one year, which may be extended for up to two additional years upon application to the Federal Reserve.

The Volcker Rule also bars certain transactions with affiliated covered funds ("**Super 23A Provision**"), by requiring that any banking entity that sponsors a covered fund, any investment adviser to a covered fund (even if it does not otherwise sponsor the fund), and any affiliates of the banking entity sponsor or investment adviser may not enter into a transaction with the covered fund that would be a "covered transaction" as defined under Federal Reserve Act Section 23A.

Need for Recalibration

Core Principles (a) and (f)

The Volcker Rule's prohibition against ownership interests or sponsorship in hedge fund or private equity funds has imposed unnecessary costs on bank-affiliated asset managers that significantly exceed any U.S. financial stability benefit, has unnecessarily reduced the ability of bank-owned asset managers to offer comprehensive investment options, and has significantly complicated compliance programs for banks providing services to investment funds, such as global custodians. Rather than protecting investors, we believe these requirements are confusing and costly to investors, outweighing any perceived benefit.

Definition of "covered funds." The definition created in the final rules is overly broad and captures many funds that are in no way "similar" to hedge funds or private equity funds.

"Naming Prohibition." The regulatory interpretation of the Volcker Rule incorporates the Federal Reserve's expansive view of what constitutes "control," for purposes of the BHCA and therefore, "banking entity" and "subsidiary" of a banking entity captures a broad range of entities within the bank holding company structure, including investment advisers in which the bank holding company may indirectly hold a minority (but above the BHCA control threshold) interest. As a result, the "naming prohibition" extends to separately incorporated investment advisers within the bank holding company structure that manage covered funds even if the investment adviser has a different name than its affiliated bank. Extending the name sharing prohibition to all covered banking entities, including to affiliates and subsidiaries of insured depository institutions and bank holding companies, provides no additional protection to investors, while creating significant economic burdens and competitive disadvantages for asset managers subject to the Volcker Rule.

Seeding of investment strategies. Seeding of investment strategies is essential to efficient and transparent introduction of new investment funds by an asset manager. The Volcker Rule, as implemented, makes it exceedingly difficult for a bank-affiliated asset manager to seed and test new strategies, due to the 3% statutory limits on bank ownership, the unduly short and burdensome requirements around temporary seeding, and the lack of clarity on use of bank assets to fund separate account seeding structures under the proprietary trading rules.

Super 23A. The final rule disrupts traditional custody banking services by, under the "Super 23A" provision, preventing custody banks from providing overdrafts or other routine extensions of credit to any "covered funds." Traditional custody services require the ability to make such routine

extensions of credit. This overly conservative interpretation of the Volcker statute: (1) Prohibits asset managers from using an affiliated custodian for "covered funds;" (2) Requires extensive compliance programs to ensure that a custodian does not on-board any investment fund customer that could technically trigger "covered fund" status under the rule's flawed definitions; and (3) Requires custodians to seek structural changes to certain customers' investment funds, particularly those overseas, in order to provide ordinary custody services.

Proposed Solutions

Congress should repeal the Volcker Rule. To the extent a full repeal is infeasible, Congress should consider replacing Volcker with tailored requirements, limiting the covered fund provisions to (1) funds that principally engage in proprietary trading; and (2) maintain the prohibition on bailing out sponsored covered funds.

AMG also supports any tailored legislative fixes that address the Volcker problems outlined above, which may have a greater likelihood of passing in Congress. To address the covered funds definitional issue, Congress should consider language that would limit the scope of the covered funds provisions to Section 3(c)(1) or 3(c)(7) funds that are principally engaged in impermissible proprietary trading by changing the definition in the statute. Congress could address the seeding issue by extending the initial seeding period to three years to ensure funds have the ability to establish track records for covered funds. A limited legislative fix could also remove the unnecessary restrictions on asset management activities, including the name-sharing restriction and limitations on investments by employees, directors, or officers who directly or indirectly provide services to a sponsored covered fund, given that the policy behind these restrictions was covered by the no bail out provision. For example, in the last congressional session, the House voted 395-3 in support of HR 4096, "The Investor Clarity and Bank Parity Act," which included narrowly tailored language that would have addressed the naming prohibition issue.

While ultimately a legislative solution is necessary, the regulatory agencies should also make regulatory changes to alleviate the immediate consequences of the Volcker rule requirements, including:

- **Definition of Covered Funds.** Narrowing the definition of "covered funds" to exclude from the definition of covered funds vehicles that are not principally engaged in impermissible proprietary trading, such as venture capital, infrastructure, and credit funds.

- **Seeding of Investment Strategies.** The regulatory agencies should automatically grant the permitted two-year extension for seeding (beyond the initial one-year) for all bank investments in covered funds and clarify that the use of bank assets to seed investment strategies for the purpose of demonstrating investment performance is not short-term trading for the purposes of the Volcker Rule's proprietary trading restrictions.

- **Naming Prohibition.** The regulatory agencies should issue guidance that states that they will not enforce this provision, pending enactment of a legislative fix.

- **Super 23A.** In addition to correcting the definition of "covered fund," regulators should amend the rule or issue guidance establishing that credit exposures extended in the ordinary course of providing custody services are not prohibited by the Super 23A provisions.

G. ETF Approval Process

ETFs have grown exponentially in popularity in recent years, with more than 1,800 funds and over $2.7 trillion in holdings.[95] Due to their structure, they have lower costs and intraday liquidity, which make them an attractive alternative to a mutual fund. Yet, despite their popularity, the SEC has yet to issue rules specifically governing ETFs.

Therefore, ETFs are forced to operate under regulations and laws written for traditional open-end mutual funds, which operate differently. Under this regulatory regime, every new ETF sponsor must obtain individualized approval, or "exemptive relief" from the SEC prior to launching its first ETF. The process is burdensome and inflexible, involving both the SEC's Division of Investment Management and Division of Trading and Markets, and often takes several months to a year to complete. Firms that mimic existing fund strategies get approved more quickly than firms that are seeking to introduce a more complex ETF, or an ETF with features that the SEC staff has not seen before. This long process significantly hampers innovation for managers, who are looking to launch new products in order to outperform the market for their clients.

Further, given that SEC standards and requirements have changed over the years, some ETF sponsors are subject to more onerous restrictions than others, which puts some asset managers at a competitive disadvantage by allowing certain market participants to engage in conduct simply because they sought regulatory relief at a particular historical point in time, while other market participants are not permitted to engage in that same conduct current-day.

Need for Recalibration

Core Principles (g)

SEC staff has been considering an ETF rulemaking since 2008, which would reportedly streamline the process and level the operational playing field for ETF sponsors. This rulemaking would be very helpful, lowering barriers to entry for many asset managers. It would also assist the SEC in better regulating and monitoring ETFs, while encouraging the industry to develop new products.

It would also be helpful if the proposed rule addressed transparency concerns, permitting with certain restrictions the ability for active managers to launch non-transparent ETFs. Currently, ETFs are required to disclose their full portfolio of holdings each day, which has been a significant deterrent for active managers who are seeking to outperform the market. By disclosing the portfolio's holdings, the manager is opening itself up to front-running or strategy replication by

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[95] Dave Michaels, *Here Come ETF Regulations (and Why the Industry is Happy About it)*, The Wall Street Journal, (Mar. 6, 2017), https://www.wsj.com/articles/here-come-etf-regulations-and-why-the-industry-is-happy-about-it-1488770041.

observant competitors, which could harm the investors in the manager's mutual funds using a similar strategy, in addition to the investors in the ETF. The SEC has considered and either shelved or rejected applications for permission to launch "opaque" actively-managed ETFs. This has effectively limited actively managed strategies to the mutual fund structure, limiting investor choice, stifling innovation, and likely affecting ETF costs.

Proposed Solutions

The SEC should issue its proposed rule that would fast track "plain vanilla" ETF approvals, and authorize by individual application non-transparent actively-managed ETFs. Additionally, the SEC should have one standard for exemptive relief that applies to all market participants.

H. Leadership of International Standards and Regulatory Harmonization

U.S. leadership of international standard-setting bodies – including the BCBS, Committee on Payments and Market Infrastructures ("**CPMI**"), FSB, and IOSCO – have been and should continue to be an important part of ensuring that regulation of markets and market participants are harmonized and consistent with U.S. standards. Most of the largest asset managers are U.S.-based and have global activities. The more that international rules are harmonized, the better it is for these U.S.-based firms. Harmonized global rules – preferably based on U.S. standards, but sometimes based on 'mutual recognition' – creates a potential competitive advantage, or at minimum a level playing field, for U.S.-based firms. Regulation of key markets, including standards for international markets such as derivatives, requires coordination and alignment in order to avoid redundancies, conflicts, inefficiencies, and impossibilities that impact access, liquidity and costs. In addition, prudential regulations (as discussed above) directly imposed upon banks have significant consequences upon markets, and thus on U.S.-based market leaders, which must be considered and right-sized.

Strong advocacy by the U.S. representatives of these international bodies to align international standards with domestic policy is particularly important, given the makeup of some international bodies such as the FSB. The FSB comprises representatives from all of the G-20 countries, including Russia and China. In voting power, European FSB members outweigh others, because they have representation at both the national and the supranational level. Regarding U.S. representation, the Federal Reserve plays a key role, serving as the Chair of the FSB Shadow Banking Workstream.

At times in the recent past, U.S. involvement in setting international standards has resulted in policy decisions that were not supportive of strong and efficient U.S. markets or of the competitiveness of U.S-based global firms, which is inconsistent with the Core Principles. The FSB and IOSCO have focused on the asset management industry, recommending policies that conflict with multiple Core Principles, for example by undermining the ability of U.S. firms to compete (e.g., G-SIFI designation would have only impacted U.S. firms),[96] and impeding regulatory

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[96] Committee on Capital Markets Regulation, *Nothing But the Facts: FSB-IOSCO Proposal for SIFI Designation*, http://www.capmktsreg.org/wp-content/uploads/2015/03/2015-03-24_Nothing_But_the_Facts_FSB_asset_managers.pdf (last visited Apr. 28, 2016).

accountability.[97] Europe has also implemented regulatory changes, such as the dealing commission restrictions under MiFID II, which are setting up direct regulatory clashes between the E.U. and the U.S. regulatory regimes. In this case, cross-border concerns have not been addressed, and absent regulatory relief by U.S. regulators, U.S. based broker-dealers will be forced to curtail providing research or execution services to asset managers, which will ultimately negatively impact investors. At other times, U.S. regulators have either ignored the global impact of their rules, or failed to work cooperatively with European Union and other regulators to agree on common standards, even where the lack of agreement could result in either lower global standards or – worse – conflicting rules that hindered the ability of U.S.-based firms to operate and meet the needs of their clients globally.

Need for Recalibration

Core Principles (d), (e), and (f)

AMG has consistently supported the FSB's role in promoting coordination and information exchange among authorities responsible for financial stability and the role of the FSB, CPMI, and IOSCO to harmonize capital markets regulations. At the same time, AMG firmly agrees with the Core Principle to prioritize American companies and American interests in international financial regulatory negotiations and meetings. However, unless U.S. regulators consistently act in coordination, with transparency and accountability to the American people, American companies and the U.S. economy could be disadvantaged.

All regulators and policymakers must prioritize harmonizing laws and regulations around the globe. Such harmonization is essential to ensuring that businesses and the economic growth they generate are not hamstrung by conflicting or inconsistent policies and to prevent costly, unnecessary, and inefficient requirements on asset management businesses, their clients (e.g., retail investment funds and pension funds), and capital markets more broadly. The FSB could be instrumental in these areas. It should not, however, be focused on addressing non-existent systemic risks in the asset management industry or influencing U.S. regulators to implement "one-size-fits-all" regulation that does not advance the Core Principles.[98]

At the same time, we recommend strengthening transparency of international processes that influence the direction of U.S. domestic regulations. Other countries cannot play an outsized role in

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[97] "Despite subsequent assertions by some of the [FSOC]'s members that the FSB and [FSOC] processes are separate and distinct, they are in my mind very much interconnected and not dissimilar." (emphasis in original), Roy Woodall, *View of the Council's Independent Member Having Insurance Expertise*, http://www.pciaa.net/docs/default-source/industry-issues/views-of-s-roy-woodall-j.pdf?sfvrsn=2 (last visited Apr. 25, 2017); *see also* Letter from Scott Goebel to the FSB, (Mar. 25, 2015), http://www.fsb.org/wp-content/uploads/Fidelity-Management-and-Research-Company.pdf (outlining many reasons why U.S. regulators should not do internationally what they cannot do domestically).

[98] *See* Financial Stability Board, *Policy Recommendations to Address Structural Vulnerabilities from Asset Management Activities*, (Jan. 12, 2017), http://www.fsb.org/wp-content/uploads/FSB-Policy-Recommendations-on-Asset-Management-Structural-Vulnerabilities.pdf and SIFMA AMG Response Letter (Sept. 21, 2016), http://www.sifma.org/issues/item.aspx?id=8589962265.

international regulatory efforts that affect U.S. markets and U.S. companies, especially since seventeen of the twenty largest asset managers in the world are U.S. based, and all of the largest funds are U.S. based. It is in the interests of the U.S. (and our global firms) to engage even more deeply in international standard-setting bodies and coordinating forums (including the FSB, IOSCO and the Joint US-EU Financial Regulatory Forum). These entities should play a key role in addressing issues such as mutually-acceptable standards for derivatives clearing, and the dealing commissions concern outlined above. Instead of allowing those bodies and forums to focus on the wrong issues, and countenance inadequate standards or standards that disadvantage U.S.-based firms (such as by adopting inadequate or conflicting rules, or rules that discriminate against U.S. firms), the U.S. should lead the way in setting appropriate, principles-based standards, both for substantive conduct and cross-border harmonization, which ideally are crafted by U.S. regulators and in any case are consistent with U.S. regulatory requirements.

While international coordination is vital, international bodies cannot supersede or supplant the role of U.S. regulators and U.S. transparency requirements, including the Administrative Procedure Act, in setting regulatory standards. For example, as discussed above, last year the FSB issued a Consultation on *Proposed Policy Recommendations to Address Structural Vulnerabilities from Asset Management Activities,* which was recently finalized. IOSCO has now been tasked with operationalizing many of the recommendations, which fall in the areas of liquidity management, leverage, stress testing, operational risk practices, and securities lending. While we supported the objectives of certain recommendations, we believed it was inappropriate for the FSB to be considering these issues *while national securities regulators were considering and seeking comment on the very same issues*. This is particularly true when considering U.S. securities regulators, which regulate the largest asset management industry in the world.

Proposed Solutions

AMG proposes recommendations on the international level that will effectuate and not undermine our domestic recommendations above. We also recommend a formal recalibration of U.S. participation in these international regulatory groups.

Given the interconnected nature of the financial markets, AMG firmly believes that the U.S. should not only continue to participate in these international bodies, but also should take an *increased* leadership role. We also believe that the U.S. should lead international regulatory efforts related to asset management and the capital markets, including current efforts at IOSCO to operationalize the FSB's recommendations, given that the recommendations will significantly impact U.S. firms, markets, and investors.

The U.S. should consider whether the promulgation of international recommendations follows a sufficiently transparent process and whether, in some cases, the international efforts undermine U.S. administrative standards and cost-benefit analysis that must be met for U.S. regulations.[99] Transparency and accountability are just as important in these international regulatory

[99] Evidence continues to mount that many of these regulatory efforts are doing more harm than good, which would be addressed through a thorough cost-benefit analysis. *See, e.g.,* BIS Report, Committee on the Global

bodies as they are domestically given the role that international standards have in influencing U.S. domestic policy.

While international coordination is important, it should not supplant the role and processes of U.S. regulators domestically.[100] U.S. regulators should be held accountable to Congress and the American public when representing the United States in international negotiations, and they should not be able to do internationally that which they are not able to do domestically. When U.S. regulators participate in international efforts to develop standards, recommendations or agreements internationally that are then passed down to the national level for implementation. These international efforts, however, cannot bypass our regulatory process. As such, the U.S. should reject implementing international standards under such circumstances.

While we are not suggesting that the U.S. should back away from ongoing international initiatives (particularly, efforts to harmonize rules in order to facilitate cross-border activity) that are already underway, we do believe that finalized, ongoing, and contemplated international regulatory efforts should be reviewed and adjusted to align with the Core Principles. To the extent that an international standard, recommendation, or principle currently under consideration by an international body or not yet addressed in jurisdictions domestically does not align with the Core Principles, the U.S. should advocate forcefully for the international regulatory body to either withdraw or amend it to address the United States' concern. The United States should also ask international bodies to stay their regulatory efforts until key leadership of U.S. regulatory agencies are in place to engage international bodies and prioritize America's best interests.[101] Once leadership is in place, we would also support a full review of existing international projects, considering President Trump's Core Principles.

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Financial System, CGFS Papers No. 59, Repo Market Functioning (Apr. 2017), http://www.bis.org/publ/cgfs59.pdf.

[100] Letter from Scott Goebel to the FSB (Mar. 25, 2015), http://www.fsb.org/wp-content/uploads/Fidelity-Management-and-Research-Company.pdf.

[101] To this end, we support House Financial Services Committee Vice Chairman Patrick McHenry's letter to Federal Reserve Chair Janet Yellen, which called for the Federal Reserve to cease all attempts to negotiate international agreements until President Trump has had an opportunity to nominate and appoint officials that prioritize America's best interests, assuming that "ceasing negotiation" will cause the international regulatory efforts to pause, rather than other countries proceeding with the efforts without U.S. engagement. Letter from Patrick McHenry to Chair Yellen (Jan. 31, 2017), https://ftalphaville-cdn.ft.com/wp-content/uploads/2017/02/02155349/McHenry-letter-to-Yellen1.pdf.

AMG sincerely appreciates the opportunity to comment and your consideration of these views. We stand ready to provide any additional information or assistance that might be useful. Please do not hesitate to contact either Timothy Cameron at 202-962-7447 or tcameron@sifma.org; Lindsey Keljo at 202-962-7312 or lkeljo@sifma.org; or Laura Martin at 212-313-1176 or lmartin@sifma.org, with any questions.

Sincerely,

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Appendix – Glossary of Defined Terms

Term/Acronym	Definition
40 Act	Advisers Act and the Investment Company Act in 1940
Advisers Act	Investment Advisers Act of 1940
AMG	Asset Management Group
ASF	Available Stable Funding
BCBS	Basel Committee on Banking Supervision
BIC Exemption	Best Interest Contract Exemption
BIS	Bank for International Settlements
CCP	Central Counterparties
CEA	Commodity Exchange Act
CFTC	Commodity Futures Trading Commission
Code	Section 4975(e) of the Internal Revenue Code of 1986
Core Principles	Principles outlined in the Executive Order
Covered companies	Banking organizations with $50 billion or more in assets
CPMI	Committee on Payments and Market Infrastructures
CPO	Commodity Pool Operator
DOL	U.S. Department of Labor's Employee Benefits Security Administration
Dodd-Frank	Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010
ERISA	Employee Retirement Income Security Act of 1974
ESIGN	Electronic Signatures in Global and National Commerce Act
ETFs	Exchange Traded Funds
Executive Order	President Trump's Executive Order on Core Principles for Regulating the United States Financial System
FCMs	Futures Commission Merchants
FDIC	Federal Deposit Insurance Corporation
federal banking agencies	Federal Deposit Insurance Corporation, Federal Reserve Board of Governors, and Office of the Comptroller of the Currency
Federal Reserve	Board of Governors of the Federal Reserve System
FINRA	Financial Industry Regulatory Authority
FSB	Financial Stability Board
FSOC	Financial Stability Oversight Counsel
G-18	18 major global banks
Gallagher Speech	Commissioner Daniel M. Gallagher, *Bank Regulators at the Gates: The Misguided Quest for Prudential Regulation of Asset Managers*,
G-SIBs	U.S. Global Systemically Important Banking Organizations
IAA	Investment Adviser Association
IOSCO	International Organization of Securities Commissions
MAT	Made Available to Trade

Term/Acronym	Definition
NFA	National Futures Association
NSFR	Net Stable Funding Ratio
OCC	Office of the Comptroller of the Currency
OFR	Office of Financial Research
OTC	Over-the-Counter
QFCs	Qualified Financial Contracts
Reg AT	Regulation Automated Trading
Reg SCI	Regulation Systems Compliance and Integrity
Regulated Funds	Reference to SEC proposed rulemaking to regulate the use of derivatives by registered investment companies and business development companies.
ROE	Return-on-Equity
RSF	Required Stable Funding
SCCL	Single-Counterparty Credit Limits
SEC	Securities and Exchange Commission
SEFs	Swap Execution Facility
SFT	Securities Financing Transaction
SIFI	Systemically Important Financial Institution
SIFMA	Securities Industry and Financial Market Association
SIFMA AMG/IAA Letter	SIFMA AMG Comment Letter to the SEC on Asset Management and Financial Stability
SLR	Supplementary Leverage Ratio
SRR	Special Resolution Regimes
Super 23A Provision	The Volcker Rule restricts transactions with affiliated covered funds
TBA	To-Be-Announced
TOB	Tender Option Bond
Treasury Report or Report	Report the U.S. Department of Treasury is developing in response to President Trump's Executive Order on Core Principles for Regulating the United States Financial System
Treasury	U.S. Department of the Treasury