

# The Systemic Risk Council

Brent J. Fields,  
Secretary  
Securities and Exchange Commission  
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## SUBMITTED VIA ELECTRONIC MAIL

August 7, 2015

**Re: Proposed Rule, Amendments to Form ADV and Investment Advisers Act Rules [Release No. IA-4091; File No. S7-09-15]**

Dear Secretary Fields:

The Systemic Risk Council (the “Council” or “we”)<sup>1</sup> is grateful for the opportunity to comment on the proposed amendments to Rules 202(a)(11)(G)-1, 203-1, 204-1, and 204-2<sup>2</sup> under the Investment Advisers Act of 1940, as amended (the “Advisers Act”),<sup>3</sup> and to Form ADV<sup>4</sup> under the Advisers Act, recently issued by the Securities and Exchange Commission (the “Commission”) in a notice of proposed rulemaking (the “Proposed Rule”).<sup>5</sup> We applaud the Commission for taking an important step toward bridging data collection gaps in the asset management industry, particularly where the industry potentially poses unique systemic risks not specifically addressed by the post-crisis financial reforms.

In a recent comment letter to the Financial Stability Oversight Council (the “FSOC”), we supported the FSOC’s efforts to expand the collection of asset management-related information from its member agencies and other federal and state authorities and offices.<sup>6</sup> In particular, we encouraged the FSOC to “devote substantial resources to improving the data-collection and modeling capabilities of the FSOC and the [Office of Financial Research] in the interests of building an effective ‘early-warning’ system.”<sup>7</sup>

Our prior letter detailed a number of areas in which the Council believes that greater data collection efforts and, in some instances, additional regulatory measures would be beneficial, including:

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<sup>1</sup> The independent, non-partisan Systemic Risk Council ([www.systemicriskcouncil.org](http://www.systemicriskcouncil.org)) was formed by the CFA Institute and the Pew Charitable Trusts to monitor and encourage regulatory reform of U.S. and global capital markets, with a focus on systemic risk. The statements, documents, and recommendations of the private sector, volunteer Council do not necessarily represent the views of its supporting organizations. The Council works collaboratively to seek agreement on each of its recommendations. This letter fairly reflects the consensus views of the Council but does not bind its individual members.

<sup>2</sup> 17 C.F.R. §§ 275.202(a)(11)(G)-1, 275.203.1, 275.204-1, and 275.204-2.

<sup>3</sup> 15 U.S.C. 80b *et seq.*

<sup>4</sup> 17 C.F.R. 275.203A-5.

<sup>5</sup> Commission, *Amendments to Form ADV and Investment Advisers Act Rules*, 80 Fed. Reg. 33718 (Jun. 12, 2015) (henceforth, “Notice”).

<sup>6</sup> See Comment Letter of the Council to the FSOC (Mar. 25, 2015), available at <http://www.systemicriskcouncil.org/wp-content/uploads/2015/03/SRC-Letter-to-FSOC-Re-Asset-Management-Products.pdf> (henceforth, “FSOC Comment Letter”).

<sup>7</sup> *Id.*, at 1-2.

- ***Documenting the degree of interrelationship between the asset management industry and the banking sector***, including information on the types of asset managers and investment vehicles that hold bank liabilities, the amount of such holdings, the concentrations of such liabilities within the industry, and the potential impact of the failure of a large bank on managed funds, as well as the overall counterparty and investment exposures of banks to asset managers and the funds they manage;
- ***Exploring the consequences of the use of leverage by asset managers***, particularly in the context of derivatives use;
- ***Examining liquidity and redemption provisions***, with an emphasis on measures to ensure the sufficiency of liquid assets during times of financial distress;
- ***Understanding securities lending and repurchase agreements***, especially the liquidity needs that may arise from such activities under stressed circumstances;
- ***Collecting data with respect to the risks of separately managed accounts***, particularly where an asset manager handles an account for a single client or a limited number of clients; and
- ***Considering the risks of regulatory arbitrage between the banking and managed funds sectors***, in light of the Commission’s recent rules imposing a floating net asset value for certain money market mutual funds.<sup>8,9</sup>

We commend the Commission for its continued commitment to improving our knowledge of the systemic risks posed by the asset management industry. Relatively little information is currently collected on separately managed accounts,<sup>10</sup> and we appreciate that the Commission cited our prior letter in proposing amendments to Form ADV that would greatly expand the agency’s collection of specific information regarding such accounts.<sup>11</sup> If adopted, the amendments would expand information collection as to the types of assets held in separately managed accounts, including the approximate percentage of regulatory assets invested in certain asset categories, information on the use of borrowings and derivatives by advisers with over \$150 million in regulatory assets attributable to separately managed accounts, information on the concentration of assets under management with specific custodians, and other information.<sup>12</sup> Importantly, the Proposed Rule would allow for the collection of data relating to the gross notional exposure, borrowings, and gross notional value of derivatives, providing the Commission with invaluable insight into the use of derivatives and borrowings by advisers in separately managed accounts.<sup>13</sup> We agree with the Commission that the proposed amendments will “enhance [the] staff’s ability to effectively carry out [the Commission’s] risk-based examination program and other risk assessment and monitoring activities with respect to . . . separately managed accounts and their investment advisers.”<sup>14</sup>

Fully recognizing the progress that has been made, we would, however, reiterate our concern as to the relative paucity of information currently available on separately managed accounts, a concern that the

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<sup>8</sup> Commission, *Money Market Fund Reform: Amendment to Form PF*, 79 Fed. Reg. 47736 (Aug. 14, 2014).

<sup>9</sup> FSOC Comment Letter, *supra* n. 6, at 3-4.

<sup>10</sup> Notice, *supra* n. 5, at 33719 (“We currently collect detailed information about pooled investment vehicles, but little specific information regarding separately managed accounts.”). *See also id.*, at 33720.

<sup>11</sup> *Id.*, at 33719, n. 12.

<sup>12</sup> *Id.*, at 33720-1.

<sup>13</sup> *Id.*, at 33720.

<sup>14</sup> *Id.*, at 33720.

Commission shares. Specifically, we urge the Commission to require advisers to report information concerning the use of securities lending and repurchase agreements in such accounts in circumstances similar to those in which comparable information is collected on Form PF with respect to private funds.<sup>15</sup>

Further, we believe that the Proposed Rule should be modified to reinforce the “total loss-absorbing capacity” (“TLAC”) rules currently under consideration by the Financial Stability Board and the Board of Governors of the Federal Reserve System (the “Board”).<sup>16</sup> Specifically, in conjunction with the Board’s issuance of proposed and final TLAC rules, Form ADV should be amended to make clear the identities of the holders of TLAC debt instruments. With the advantage of this additional information, markets and supervisors would have a clearer understanding of the credibility of future “bail-in” scenarios. Market prices would come to reflect the differences between “strong” and “weak” TLAC holders, as only the former provide a robust loss buffer and thus obviate the need for government intervention. Supervisors, moreover, could use this information to confirm whether TLAC holders are adequately equipped to survive a potential bail-in event without material damage to their business models. By increasing transparency and allowing for more targeted supervision, this relatively minor adjustment to Form ADV would contribute significantly to efforts to reduce systemic risk.

In addition, we repeat our concerns as to the interrelationships between the asset management industry and the banking sector, the relationship between redemption provisions and liquidity, and the systemic risks inherent in the securities lending and repurchase agreement activities of asset managers. We recognize that to address these issues fully, coordinated action with other regulators will be necessary. However, we encourage the Commission to consider whether Form ADV could be enhanced to address these fundamental systemic risk issues at least in part.

Finally, we urge the Commission, as it evaluates the data to be gathered through enhanced filings under the Proposed Rule, to focus on the use of leverage by asset managers and the risk of regulatory arbitrage between the banking and managed fund sectors.

Thank you very much for your consideration.

Respectfully submitted,



Sheila Bair, Chair  
On behalf of the Systemic Risk Council  
[www.systemicriskcouncil.org](http://www.systemicriskcouncil.org)

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<sup>15</sup> Form PF, which is filed by certain registered investment advisers, provides for standardized monthly reporting of various financial information regarding advisers and the funds they advise. Such information includes the amount and type of such qualifying hedge fund borrowing (*e.g.*, unsecured, reverse repurchase agreements, and dedicated liquidity facilities), the amount and type of collateral pledged, and the types of counterparties. *See* 17 C.F.R. § 279.9; *see also* Commission Form PF, “Reporting Form for Investment Advisers to Private Funds and Certain Commodity Pool Operators and Commodity Trading Advisors,” available at <http://www.sec.gov/about/forms/formpf.pdf>.

<sup>16</sup> *See, generally*, Comment Letter of the Council to the Financial Stability Board (Feb. 2, 2015), available at <http://www.systemicriskcouncil.org/wp-content/uploads/2015/02/SRC-TLAC-Comment-Letter-to-FSB-020215.pdf>.

## Systemic Risk Council Membership

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- Nout Wellink, Former President of the Netherlands Central Bank and Former Chair of the Basel Committee on Banking Supervision Settlements

\* Affiliations are for identification purposes only. Council members participate as individuals, and this letter reflects their own views and not those of the organizations with which they are affiliated.