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September 6, 2016

Submitted via electronic filing: www.sec.gov/rules/proposed.shtml

Mr. Brent J. Fields
Secretary
US Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: Adviser Business Continuity and Transition Plans, File Number S7-13-16

Dear Mr. Fields:

This letter responds to the request of the Securities and Exchange Commission ("Commission" or "SEC") for comment on topics covered by the proposed rules regarding Adviser Business Continuity and Transition Plans ("Proposal").[1] BlackRock, Inc. (together with its affiliates, "BlackRock")[2] is supportive of the Commission's goals and views Business Continuity Management ("BCM") planning as a critical function for investment advisers. To this end, we are supportive of the Commission's goals of ensuring that investment advisers have in place policies and procedures designed to mitigate the impact of business disruptions that could affect their ability to continue providing investment management services to their clients.

Investment advisers span a broad range of different business models, meaning that a "one-size-fits" all approach is unlikely to address the unique business continuity and operational risks to which an individual investment adviser is subject. As such, we encourage the Commission to maintain a principles-based approach to ensure that the final rule and its implementation can result in the development of policies and procedures that are broadly applicable to the diverse range of adviser business models under the Commission's purview. Further, as the Commission is well-aware, technology and market practices will continue to evolve over time, which could result in the emergence of new and/or different business continuity risks for investment advisers. As such, pursuing a principles-based approach will permit the final rule to stand the test of time and adapt to the constantly changing environment in which investment advisers operate.

In addition, we would like to emphasize that we view BCM and transition planning as separate and distinct concepts, with different objectives. More specifically, BCM is focused on the resumption of business, while transition planning is focused on the wind-down of a business. As a result, BCM policies and procedures are regularly invoked by investment advisers for a variety of reasons, including natural disasters (earthquakes,

1 SEC, Adviser Business Continuity and Transition Plans, 81 Fed. Reg. 43530 (July 5, 2016), available at https://www.gpo.gov/fdsys/pkg/FR-2016-07-05/pdf/2016-15675.pdf ("Proposal").

2 BlackRock is one of the world's leading asset management firms. We manage assets on behalf of institutional and individual clients worldwide, across equity, fixed income, liquidity, real estate, alternatives, and multi-asset strategies. Our client base includes pension plans, endowments, foundations, charities, official institutions, insurers, and other financial institutions, as well as individuals around the world.

hurricanes, floods, tsunamis) and for man-made issues (terrorism, electrical failure, etc.). By contrast, transition plans would be highly unlikely to ever need to be used. While there may be some overlap in certain circumstances, commingling these concepts with disparate objectives into a single set of policies and procedures would at the very least be confusing to employees or potentially counterproductive to the adviser and the Commission. To this end, we recommend the Commission separate these concepts in the proposed rule or even consider separating the provisions of each Proposal into two separate rules. As such, we have treated BCM and transition planning separately throughout this response letter.

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Executive Summary

<u>Business Continuity Management</u>

We commend the Commission for being proactive about BCM risks and for seeking to set minimum standards in the industry in order to protect all investors. We agree with the Commission that all advisers should have BCM policies and procedures in place. Business continuity risk includes risks that can arise from business disruptions resulting in the loss of facilities, systems, and the unavailability of personnel to perform their duties. All asset managers should, and most already do, have BCM programs in place to address business continuity risks. However, it is important to note that having a BCM program is not the same as having a single Business Continuity Plan ("BCP"). A BCM program allows for separate ownership of key program components and different sets of policies and procedures related to business continuity planning. For instance, an operations team would maintain procedures to recover systems and data, a trading team might maintain plans to transfer trading capabilities to alternate locations or recovery sites, and a compliance team would likely maintain policies regarding notifying regulators. The requirement for a BCP could be interpreted to mean that one plan document needs to govern a variety of business units; rather, we see BCM as involving procedures that different business units call upon when a potential disruption occurs. Efforts to ensure good BCM practices should focus on a comprehensive program, recognizing interconnectivity of business units as opposed to attempting to put all business continuity plans into a single document.

The specifics of BCM programs necessarily vary based on each adviser's unique business model (e.g., product types, geographic focus, outsourcing of one or more operational functions, single location, multiple locations). In addition, BCM programs are dynamic and updated constantly. Regular review and updating is considered a best practice with respect to BCM. This includes changing procedures when there is a change to the business model (e.g., opening new office locations) or innovations in technology (e.g., ability to work remotely).

Our main recommendations related to BCM are as follows:

1. *We encourage the Commission to balance the need for minimum BCM standards with the need for flexibility to tailor BCM policies and procedures to each investment adviser's unique business model. To this end, we strongly urge the Commission to ensure that the final rule takes a principles-based approach to BCM instead of prescribing specific granular details of BCM programs.*

2. *Given the diversity of business models in the asset management industry, we recommend that the Commission require registered advisers to have a BCM program, including one or more BCPs.*

This program should include at a minimum elements that address the following principles identified by the Commission:

(i) Maintenance of critical operations and systems, and the protection, backup, and recovery of data;
(ii) Communications with clients, employees, service providers, and regulators; and
(iii) Identification and assessment of third-party services critical to the operation of the adviser.

We believe that advisers should have the flexibility to implement these principles in the manner that is most appropriate for their business given the diversity of business models used in the industry. In other words, how each principle is implemented, e.g., through which policies and procedures, what types of back-up arrangements, forms of communication, etc. will likely vary from adviser to adviser and should be tailored to the business model, size, complexity, geographic location, and a number of other aspects of the adviser's business.

3. *We are concerned that some of the proposed provisions are too granular and may not stand the test of time or be applicable to all business models.*

For instance, we recommend that the Commission clarify that the requirement to have a pre-arranged alternate physical location(s) can be satisfied with the existing offices of a firm with multiple offices and the capacity for remote access. By making a prearranged location a requirement, the Commission is dictating how advisers recover, not that advisers are able to recover. While having a prearranged alternate location may be sensible for a manager with a single office, it is less relevant for managers with multiple offices that are geographically dispersed. For example, we have often implemented BCPs by transferring work to alternate offices and/or working remotely. That said, there are times when BlackRock may utilize recovery sites. The decision on which approach to take is based on the facts of the situation and is virtually impossible to pre-determine. For example, during Winter Storm Juno, our New York region-based employees were able to work from home and transfer work to locations globally. While we maintain recovery sites in some of our locations, these are based on specific local risks and are not an expectation or requirement for our baseline program for all locations.

4. *We agree with the Commission that understanding and verifying that service providers have BCM programs is an important part of an adviser's business practices.*

The Commission should clarify that advisers have satisfied the principle regarding the identification and assessment of third-party services critical to the operation of the adviser as long as they engage in ongoing due diligence of the BCM programs of their service providers, which is good vendor management. Liability is best placed with the service providers for inadequacies in their programs, as asset managers can conduct diligence but do not ultimately control such programs. Advisers should be expected to discuss BCM programs with service providers, and the extent of back-up arrangements must be proportional to the materiality of that service provider to the adviser's business. Only the adviser can make this determination. The Commission should require advisers to consider service providers when making their own BCM programs, but beyond this general principle, we do not believe that any further requirement is practicable.

5. *We agree with the Commission that advisers should have discretion as to which business disruptions warrant notification to the Commission.*

The invocation of BCPs by business units is a normal occurrence and a significant number of events requiring use of BCM procedures occur on a regular basis. These procedures are often utilized to ensure that there is no disruption to business, not because the business has been disrupted. To put this in perspective, recent examples where BlackRock business units invoked aspects of our BCM and did not experience any business disruption include: typhoons in Japan, a power outage in Seattle, and transit strikes in New Jersey and Scotland. Advisers should be able to determine when a disruption is sufficiently material to warrant notification to the Commission.

6. *We agree with the Commission that advisers should conduct annual review of BCM programs, and believe that the record of such reviews need only indicate the individuals that conducted the review during the last year.*

The actual changes to the policy or procedure that is part of the BCP should be reflected in the new BCP. Good business practices and current regulation include reviewing and updating BCPs continuously—at least annually, as is done currently with compliance procedures that include BCP as a component. BCPs are updated regularly due to a variety of factors, such as personnel changes. As such, retaining old documents that no longer accurately describe BCM policies, procedures, and responsibilities would not serve any regulatory purpose and could make the process of updating BCM plans unnecessarily cumbersome.

7. *BCM program documents should not be made public or filed with the Commission.*

Individual business continuity plans and overall BCM program documents should be treated confidentially, as (i) they contain details about a firm's business operations that could be used to support illicit behaviors such as cyber-crime and (ii) they contain personally identifying information ("PII") of the firm's staff. Filing hundreds of BCM policies and procedures with the Commission would not serve any regulatory purpose and would make amendments more burdensome.

<u>Transition Planning</u>

Investor protection and financial stability are important goals for regulators and investors alike. We agree with the Commission's view that "The rapid recovery and resumption of the financial markets and activities that support them underpins the resiliency of the US financial system."[3] Further, we agree with the notion that an investment adviser's fiduciary responsibility extends to situations where an adviser transition is taking place. However, as the Proposal notes, actual experience

[3] Proposal at 43532.

demonstrates that investment advisers who stumble do not "fail" suddenly, but rather may fade away over time. This is in contrast with other types of financial services firms, which, as the Commission rightly notes, can and have experienced situations where there was a need to exit a business suddenly and quickly. These differences stem from the fact that the businesses that investment advisers are in do not lend themselves to the sudden failure situations in which other financial services firms whose daily operations rely on access to short-term wholesale funding and highly leveraged balance sheets can find themselves. As such, it is important to take into account the reality of how investment adviser transitions generally occur into any guidance or rules regarding transition planning for investment advisers and ensure that transition planning by investment advisers is relevant and tailored to the business models of investment advisers.

Further, it is important to consider transition planning for investment advisers in the context of the existing regulation of various products and services. For example, the Investment Company Act of 1940 ("1940 Act") already has provisions for replacing a fund manager by the fund's board. Likewise, the regulation of custodians—all of which are banks—already addresses concerns with respect to how client assets are safeguarded at all times, including during an adviser transition. Investment adviser transition plans cannot and should not supersede fund constituent documentation or the regulation of custodians. As such, rules that require investment advisers to create policies and procedures to address aspects of a transition that are outside of their control or where there are already pre-defined procedures and governance structures are more likely to be confusing than helpful during a transition. Care should be taken to ensure that this is not the outcome of the transition planning requirements of the Proposal.

With these themes in mind, we have made specific recommendations regarding the provisions of the Proposal below.

1. *Transition plans are highly unlikely to ever be implemented by an investment adviser because investment advisers do not suddenly cease to exist or fail. The Commission should acknowledge the low likelihood of a sudden failure of an investment adviser and ensure that any new rules or guidance are proportional to the risks involved.*

Most financial firm failures are directly related to funding risk, whether in the form of exposure to short-term funding or exposure to run risk on deposits. Investment advisers have neither of these exposures. In addition, investment advisers do not guarantee the investment results of products, nor are they counterparties to securities transactions or derivative contracts (beyond perhaps a nominal amount on behalf of the company itself).[4] Looking back over the past 30 years, we find no examples of an investment adviser suddenly ceasing to exist. In fact, actual experiences of firms and/or funds that have stumbled due to performance, reputational events, or other issues demonstrate that adviser transitions have been orderly. As detailed in Appendix A, in a variety of stress situations, client assets were successfully protected and transitioned.

[4] Like most corporations, asset managers may engage in hedging activities using derivatives. However, this is generally miniscule in comparison to the transactions executed by the asset manager on behalf of clients.

2. *Investment adviser business models are not homogeneous. A principles-based approach to transition planning is necessary to ensure that the transition planning requirement is relevant for a broad range of investment advisers.*

Investment advisers come in many shapes and sizes with multiple dimensions of diversity across the industry.[5] Areas where the business model of an investment adviser can differ widely include the capital structure of the parent company and affiliates, the asset class and product type focus, as well as the composition of the client base. Transition planning needs to take into account the characteristics of the asset manager's business model and consider potential risk factors associated with that business model. Factors to consider in this regard include: (i) intrinsic revenue stability, (ii) level of leverage or exposure to debt, (iii) ability to adjust expenses using variable compensation to allow significant decreases in revenue to be offset by decreases in expenses, (iv) the type and diversity of asset classes (e.g., equity, fixed income, cash, real estate, private equity, emerging markets, etc.), (v) the type and diversity of investment processes (e.g., active, passive, quantitative, fundamental, etc.), (vi) the diversity of the clients (e.g., retail, institutional, insurance, etc.), (vii) the number and diversity of the products (e.g., separate accounts, mutual funds, exchange traded funds ("ETFs"), alternative funds, etc.), and additional affiliated products and services (e.g., custody, valuation, recordkeeping, technology platforms, etc.). Unlike a bank, where complexity is considered an indicator of risk, in the case of an asset manager, business diversity generally improves the stability of an asset manager's revenue and is, therefore, an indication of the resilience of the firm to withstand changes in client preferences and other short-term trends that might be damaging to concentrated, single strategy businesses.

3. *With respect to the provision that would require adviser transition plans to address "policies/procedures intended to safeguard, transfer and/or distribute client assets during a transition,"[6] we highlight the important role that custodians play in ensuring the protection of client assets and note that custody rules were recently updated.*

Whether in the normal course of business or during an adviser transition, investment advisers do not own or custody client assets. Rather, custodians are tasked with protecting client assets.[7] The decision to select a custodian is the remit of separate account clients, and fund boards approve the custodian for the funds they oversee. With respect to separate accounts, in the event of an issue with an adviser, the client can take direct control of its assets, or hire a different manager – either temporarily or for a longer-term assignment. In the event of an issue with a 1940 Act fund, again the assets are protected by the custodian and the fund board can replace the investment adviser. Section 15 of the 1940 Act provides for this very situation by allowing 1940 Act fund boards to replace a manager on a temporary basis without a shareholder vote.[8] For

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5 Office of Financial Research, Asset Management and Financial Stability, 3 (Sep. 2013), available at https://www.treasury.gov/initiatives/ofr/research/Documents/OFR_AMFS_FINAL.pdf.

6 Proposal at 43556.

7 Investment advisers may have custodian affiliates, but these are generally separate legal entities and are regulated under banking and trust rules relevant to custodians.

8 15 U.S.C. § 80a-15. 1940 Act Rule 15a-4 provides that, subject to certain conditions, a fund board can appoint a new investment adviser to a fund for a period of up to 150 days without first obtaining shareholder approval of the new advisory contract. The Rule permits fund boards to appoint a new adviser in a situation where the original adviser's contract has been terminated.

private funds, those with a fund board would operate in a manner similar to that of 1940 Act funds to hire a new adviser, and those without one have contractual provisions addressing contingency scenarios where the adviser or general partner (which could be an affiliate of the adviser) goes out of business. In any event, the assets are still held at a custodian. Thus, as discussed throughout this comment letter, the custodian performs a critical function in the transfer of client assets.

4. *Existing regulation under the 1940 Act and client constituent documents often already address procedures for the wind-down or liquidation of a fund as well as the procedures for terminating and replacing the adviser. The Commission should clarify that adviser transition plans do not need to be so granular as to address the unique provisions of each client account or fund.*

Funds liquidate regularly in the normal course of business. According to the Investment Company Institute ("ICI"), 462 US mutual funds were liquidated or merged into other funds during 2015.[9] Similarly, hedge funds are launched and closed on a regular basis. According to Hedge Fund Research, 291 hedge funds closed during the second quarter of 2016 alone, down from 305 closures the previous quarter.[10] With respect to more liquid hedge funds, the sophisticated investors in these funds usually redeem over time when the fund is not performing to their satisfaction. Hedge funds generally have notice periods, gates and/or side pockets that are designed to facilitate an orderly liquidation of the fund or replacement of the adviser.

5. *One area of interest noted by the Commission is that of transitioning derivatives positions.[11] While standard transition management practice for derivatives is for the legacy manager to close positions and the new manager to open desired positions, what is convenient in the normal course is not a strict requirement. In the case of a manager transition, decisions regarding outstanding derivatives positions should be made by the client or fund board based on the client's circumstances and the market environment, not pre-determined by a transition plan.*

Given that the client is the counterparty to the derivatives transactions, it is important to ensure that the client's rights to make their own decisions about the management of their assets are respected during any adviser transition. In the extremely unlikely situation where an asset manager suddenly were to go out of business, which requires the management of uncleared derivatives positions to be transitioned quickly, it would be up to the client and the new asset manager (or the client themselves in the case where the client decides to manage their assets in-house) to determine the appropriate course of action. In such a circumstance, the client could decide that closing out and re-establishing the positions is the most efficient approach, and the new manager would follow the normal market practice. In other cases, the client could decide to close out the existing position and not to re-establish or wait until more favorable market conditions come about before doing so. Alternatively, if the client

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9 ICI, 2016 Investment Company Fact Book: A Review of Trends and Activities in the Investment Company Industry, 19 (May 2016), available at https://www.ici.org/pdf/2016_factbook.pdf.

10 Hedge Fund Research, Press Release, Hedge Fund Liquidations Edge Lower in 1Q 2016 (Jun. 16, 2016), available at https://www.hedgefundresearch.com/sites/default/files/articles/pr_20160616.pdf; Mary Childs, Financial Times, *Hedge funds culled as performance sags* (Jun. 16, 2016), available at http://www.ft.com/cms/s/0/c3be89b0-33dc-11e6-ad39-3fee5ffe5b5b.html#axzz4IHbEmH70.

11 Proposal at 43542, note 103.

decided that it did not want to terminate the position, it is possible to transfer and re-document the derivatives positions without terminating and re-establishing them. As such, the transfer of derivatives positions would be unique to the transition scenario and client wishes at the time of transition. Thus, it may be difficult to specify instructions for the transition of client derivatives positions in a pre-determined transition plan.

Importantly, as more derivative contracts move to central clearing, transferring these positions from one manager to another becomes even simpler. For example, all information would be transparent, the terms would be standardized, and a new manager could step into its agent role for an existing contract quite seamlessly.

6. *We agree that it could be helpful for advisers to have a mechanism in place that would facilitate prompt retrieval of client-specific information and other relevant contact information, such as for fund boards, service providers, counterparties, etc. In many cases, these mechanisms may already be in place.*

7. *We agree that it could be helpful for advisers to have a mechanism in place that would facilitate the prompt identification of contractual or regulatory provisions that would be implicated by a change of control of the investment adviser.*

That said, the Commission should recognize that the regulation of traditional products, such as 1940 Act funds, is well known and understood by potential replacement advisers. The Commission should clarify that for 1940 Act funds, it would be sufficient for the adviser to simply reference the 1940 Act. No further assessment should be required.

8. *Transition plan documents should not be made public or filed with the Commission.*

These documents should be kept confidential as they often contain information, such as succession plans, which may not even be widely known within the adviser organization. Moreover, filing will make them more difficult to amend as circumstances change.

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I. Investment Adviser Business Continuity Plan: Comments on Rule 206(4)-4

BlackRock agrees with the Commission that BCM planning is a critical aspect of an adviser's business. We agree that business continuity planning "supports resiliency and is one that financial services firms, including investment advisers, generally should engage in to address the inherent risks they face in serving their clients' needs."[12] We are supportive of BCM planning for the maintenance of critical operations and systems, and the protection, backup, and recovery of data; communications with clients, employees, service providers, and regulators; and identification and assessment of critical third-party service providers.

12 Proposal at 43533.

Principles-Based Approach

Given the diversity of business models for advisers, we believe that the Commission should allow advisers to adopt policies and procedures in a way that works for their individual businesses. Smaller advisers may find one BCM plan document more helpful, and thereby could retain one BCM plan document, while larger advisers may be organized by location/business units and need to maintain a BCM program with numerous individual BCM plan documents. If the Commission's requirements are too granular, they will not be well-suited to the variety of adviser business models. A principles-based approach also makes it easier to harmonize procedures globally; the ease with which BCM plans can be efficiently implemented, particularly for firms with locations in different regulatory jurisdictions, is facilitated by the application of universal principles that can be tailored by each adviser to its business model.

We believe that the Commission could easily adapt the Proposal to be principles-based by requiring advisers to take into account the following three general requirements when designing BCM programs: (i) maintenance of critical operations and systems, and the protection, backup, and recovery of data; (ii) communications with clients, employees, service providers, and regulators; and (iii) identification and assessment of third-party services critical to the operation of the adviser. The specifics of how each of these principles is to be implemented should be left to each adviser to manage according to its business model and operational structure.

The reason for our recommendation is that we believe that some of the specific requirements under the Proposal are not applicable to all advisers, and we believe that a more principles-based approach would not need to spell out requirements that are not universal in their nature. Following are examples of requirements that are not pertinent to all advisers:

(i) Pre-arranged alternate physical location(s) of the adviser's office(s) and/or employees. This should be clarified to include existing offices and remote capabilities because some advisers already have multiple offices and remote work capabilities.
(ii) The Commission is proposing to require the maintenance of critical operations for the clearing and settling of transactions. However, not all advisers conduct these activities.

We support the Commission's goal of ensuring that advisers consider issues, such as risk management and financial and regulatory reporting, in developing their BCM programs. However, we believe that requirements, such as including a centralized inventory of key documents, including the location and description of the item, and a list of the adviser's service provider's relationships that are necessary to maintaining functional operations, are too prescriptive. For some advisers, distinct business groups are responsible for preparing for different types of disruptions. What is important is ensuring that information is appropriately stored on servers that are recoverable, and requiring one centralized inventory would not be as effective for programs that are already in place and have been tested by actual events, designed effectively to manage these risks in a decentralized way.

Service Providers

The principles-based approach should be applied with respect to the Commission's requirements regarding service providers as well. We agree with the Commission that management of vendors and due diligence regarding the BCM programs of service providers is important to the business practices for advisers. We also agree that "once an adviser identifies its critical service providers, it should review and assess how these service providers plan to maintain business continuity when faced with significant business disruptions and consider how this planning will affect the adviser's operations."[13] Advisers are already required to monitor the adequacy of BCM policies and procedures for certain critical service providers under Rule 38a-1.[14] Given the fiduciary responsibility that asset managers have to their clients, it is in the best interest of asset managers to ensure that service providers have robust operational controls and can continue operations, even during times of market stress or business disruptions. We understand the Commission to be giving advisers flexibility to make their own assessments of third-party service providers on a case-by-case basis since a single standard or single definition of "critical" will not work for all advisers. The Commission assumes that if a service provider executes a particular activity – such as providing services related to portfolio management, the custody of client assets, trade execution and related processing, pricing, client servicing and/or recordkeeping, and financial and regulatory reporting – it is a "critical" service provider.[15] While we agree that these services are "critical," we do not believe that all of these service providers are "critical" to the adviser in every case. The adviser's particular business and operating model along with the substitutability of a given vendor (which is helped by competition in the vendor's industry) drive each adviser's individual determination of which service providers are "critical." The Commission should, therefore, leave the determination as to which service providers are "critical" up to the adviser, and recognize that not all providers of the same service are "critical" to an adviser's business as a whole.

Advisers should work with their service providers to discuss resiliency and BCM practices. They should review the BCPs and technology disaster recovery plans ("DRPs") of critical third party service providers, both during the initial due diligence process and then on an ongoing basis, thereafter. The level of engagement with providers will likely vary based on the services being provided and potential impact to the asset manager should the vendor's services be interrupted. Written contracts with third party service providers should clearly outline the duties, obligations and responsibilities of each such vendor. The Commission should set out broad principles regarding the identification of critical service providers and could provide guidance regarding some potential best practices, such as those we have suggested above, and leave the specific management of vendor risks to advisers, as this management will depend heavily on each adviser's business model.

The Commission should appreciate that client services can be moved from one service provider to another if needed, and transitioning services could incur additional costs. In some cases, maintaining back-up arrangements may be practical, but advisers

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[13] *Id.* at 43541.

[14] "The [compliance] procedures must provide for the oversight of compliance by the fund's advisers, principal underwriters, administrators, and transfer agents (collectively, "service providers") through which the fund conducts its activities." 17 CFR 270.38a-1.

[15] Proposal at 43541.

must have the flexibility to balance the costs of back-up arrangements against the materiality of the service provider given its own BCM program, the BCM program of the service provider, the availability of other quality service providers, and the needs of its clients.

BCM Best Practices

We believe that any rule/guidance should allow for a BCM program to deliver and scale in line with best practices and regulations that are already in place. We recommend the following BCM best practices could be used to provide guidance to asset managers on what their program should cover, without detailing how each best practice should be delivered.

- Analysis: Threat analysis to define the probability and potential impact of external threats and hazards.
- Planning: Written plans that document key tasks, outline recovery strategies, define key team members, dependencies, key third parties, and technology requirements needed to facilitate technology DRPs. The quantity and scope of these plans would be determined by organization.
- Training: Ongoing training of staff in order to ensure they understand their roles and how the firm will operate during a crisis.
- Exercises: Plans should be exercised annually to confirm the adequacy of recovery strategies, including use of remote access, recovery sites, alternate offices and transfer of critical processes.
- Governance: BCM program governance should ensure clear ownership of risk and reporting to senior stakeholders.

For instance, how BlackRock delivers these areas is outlined below:

- Analysis: Blackrock annually assesses all key sites for both internal and external risks to create a key site scorecard.
- Planning: BlackRock has numerous BCM plans, and multiple policies and procedures dealing with all aspects of our BCM planning. The plans include: (i) identification of personnel and alternative personnel for critical tasks; (ii) required applications and their criticality; (iii) critical third parties; and (iv) use of locations globally that allow us to continue providing services.
- Training: At a minimum all staff are required to take an awareness training annually. Some staff additionally receive selective trainings based on their role. These trainings may include crisis management online training and/or in-person sessions, as well as awareness sessions for those selected in BCPs to play a role in the recovery of their team.
- Exercises: All required BCM plans are practiced at least annually.
- Governance: BlackRock's BCM program relies on the firm's risk management structure and operates as a second line of defense in our three lines of defense model. In our experience, similar models have been or are being implemented by many asset managers across the industry. The three lines of defense in this model are: (i) *first line* – business units are responsible for creating and testing BCPs that are in adherence with centrally defined requirements; (ii) *second line* – a central business continuity team defines policy, oversees adherence with planning requirements, conducts quality checks and reports to management; and (iii) *third line* – internal and external

audit are responsible for auditing individual business plans as well as the overall business continuity program and framework.

Other key areas that are integral to a robust BCM program include technology DRP and crisis management, which are described below.

Technology Disaster Recovery Planning

Technology DRPs are a part of any business continuity program and include processes and procedures to recover technology systems and infrastructure that are critical to the management of client accounts. For example, while some asset managers have developed systems in-house, others purchase systems from external vendors. As such, this could result in differences in technology DRPs.

Crisis Management

Similar to BCM, we believe that firms should maintain a crisis management framework that provides a mechanism for how the firm manages a crisis when it occurs. This framework should include mechanisms for decision making and communication within an organization. As with BCM, we believe that each firm has unique structures and organization and it should be left to the firm to decide how they implement a crisis framework. In this respect, we believe that the crisis framework is the right place to consider the SEC principle around communications with clients, employees, service providers, and regulators.

When business disruptions do occur, a crisis management framework can be used to manage incidents that require coordination across multiple business lines or across multiple locations. Asset managers typically develop a framework that defines how coordination will take place during a crisis event. This includes communication and escalation procedures (across business, technology, management, etc.) as well as with clients, regulators, and other third parties. The frameworks should include local, regional, and global crisis teams that respond to and facilitate the recovery from disruptive events.

Notice to the Commission

The Commission proposes to require advisers to identify "under what circumstances it would notify" its regulator of a "significant business disruption."[16] We agree with the Commission that advisers should have discretion to determine what circumstances are sufficiently material to warrant notice to the Commission. While communications with regulators is an important part of any BCM program, we do not believe that notice to the Commission is warranted for every BCM disruption. The invocation of various aspects of BCM programs is a normal occurrence and there are a significant number of BCM events on a regular basis. BCM policies and procedures are often invoked to ensure that there is no disruption to business, not because the business has been disrupted. Recent examples where BlackRock business units invoked aspects of our BCM and did not experience any business disruption include: typhoons in Japan, a power outage in Seattle, and transit strikes in New Jersey and Scotland.

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[16] *Id.* at 43540.

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II. Investment Adviser Transition Plan: Comments on Rule 206(4)-4

We are supportive of the Commission's goal to ensure the transitioning of services even when a significant disruption causes an adviser to have to wind down its business. As discussed above and as shown in the examples in Appendix A, assets are transitioned in an orderly way even when the adviser has gone out of business. We recognize that while it is unlikely, there may be a scenario where a swift transition may be disruptive to clients if certain aspects of the adviser's business are not in good order.

The Commission requests comment on whether all advisers should have transition plans or whether only a subset, e.g., based on size, should be required to have them.[17] In addition, the Commission requests comment on whether an adviser's transition plan should be based on the complexity of its business.[18] We believe that this focus on "size" and "complexity" in asset management is misplaced. In fact, smaller firms with fewer resources present key man and succession planning issues, and single product firms can have business concentration risk issues, which increase the likelihood of the adviser going out of business. We believe that the Commission should take a principles-based approach towards transition planning for all advisers to ensure that advisers maintain their records in good order to facilitate an orderly transition, without mandating specific methods or plan documents.

<u>The Requirements of the Proposal Should be Proportional to the Risks Involved</u>

The business model of investment advisers is such that they are highly unlikely to have to wind down suddenly in a manner that would require invoking a transition plan. Funds liquidate regularly and advisers are terminated or may go out of business in the normal course. In the event of a liquidation of a fund, investors are paid redemption proceeds. These assets are not held by the adviser at any point in this process.

Importantly, as the Commission is aware, client assets are held by custodians. Furthermore, transitioning the management of a client's account need not necessarily entail the selling of assets, as client assets are segregated from the asset manager's own assets and are held by a custodian.[19] Even in the event of a sudden exit by an adviser, which is highly unlikely, client assets would not be impacted and the custodian need not change. Even if a transition were delayed or cumbersome, it still would not present systemic risk; the assets would not be in jeopardy because of the failure of an adviser.

In the case of the termination of an adviser or where an adviser goes out of business or decides to exit its advisory business, an orderly transition to a new adviser occurs in the normal course. Further, there is significant expertise regarding mergers and acquisitions in the asset management space.

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[17] Proposal at 43543.

[18] *Id.* at 43544.

[19] Note that derivative positions may be held through a different entity and not held directly by the custodian, where permissible. Nonetheless, derivative positions are not held by the asset manager.

From our experience acquiring other asset managers (both large and small, both single product and multi-product), we know that in reality, situations where advisers exit a business or sell a portion of their business to another adviser do not happen overnight. They require a transition plan unique to the situation; rendering a pre-determined transition plan document unlikely to be helpful. A transition plan for a business sale or exit must necessarily be unique to the specifics of each situation. Consequently, it is unnecessary to develop a hypothetical transition plan about a potential business sale or exit in advance of such action, without the benefit of knowing the details of any such transaction. Nonetheless, we are supportive of advisers maintaining key documents in good order in the event of such transitions. In our experience, the contractual arrangements between the legacy advisers and their clients already allow for an orderly transition to a new adviser.

As an initial matter, it is important to understand how transitions work in general under standard contractual provisions, as well as past cases of when asset managers have failed and what happened to the assets being managed. To this end, we provide below some general background on contractual provisions. In Appendix A, historical examples of the transition of services from one adviser to another are described in detail.

Contractual Provisions

Even if an asset manager were to wind down suddenly, contractual provisions provide for an orderly transition of client assets in such situations. To illustrate the point that the failure of an adviser does not lead to systemic risk, we consider the following cases of a hypothetical adviser going bankrupt or being terminated, and explain how client assets would be protected and an orderly transition would occur.

- Separate account: Under a standard investment management agreement ("IMA"), each client has the right to terminate an adviser on short notice. The client may work with an institutional consultant to make the decision to terminate, or may act independently. The client may consult a commercially available database, or may already have existing relationships with other managers. In asset management, there are multiple competitors available for virtually every investment strategy. In addition, clients may choose to manage the assets themselves or appoint an interim manager until they can do a more thorough search. We have seen every one of these scenarios occur in a variety of circumstances. Regardless of the decision process to make a change, the assets remain at the client-selected custodian. The account at the custodian remains the same and the assets are not affected unless the client decides to change strategies altogether. None of these have any implications for the existing manager's ability to transition the client's assets or present systemic risk concerns.
- Registered fund: Mutual fund clients have the right to redeem from a fund, and a manager is expected to have liquidity risk management procedures in place. In terms of protecting client assets, the fund assets are held at a custodian approved by the fund board, and the contract between the fund and the custodian would remain in place. Where a manager goes out of business, Section 15 of the 1940 Act permits a 1940 Act fund board to replace a manager on an immediate basis prior to obtaining a shareholder

vote to approve the new adviser.[20] We note in Appendix A that in several situations where a firm experienced a significant reputational event, mutual funds have been transferred to a new manager with other funds as a successful strategy for transitioning these client assets.[21]

- Private fund: Real estate, private equity and hedge funds often include lockup periods, notification periods, gates and/or side pockets in their offering documents. Under the offering rules, these products are generally offered to institutional investors and individuals who meet the definition of sophisticated investors. Some funds are closed end (such as private equity or venture capital funds); others are open-end (such as some hedge funds or some real estate products). Investors in open-end funds can submit redemption requests, and the funds handle redemptions and liquidate in an orderly way if and when required. Some funds have boards, and in these cases, boards could meet and appoint a new adviser. Less liquid funds have contractual provisions that provide for contingency scenarios in which investors may replace the general partner, which is generally an affiliate of the adviser, in case of the adviser's or general partner's bankruptcy and/or hire a liquidator to manage the liquidation of the assets. The assets of the fund are again held by a custodian, and all activity generally is monitored by a fund administrator. Hence, no client assets would be in jeopardy even if the adviser were in bankruptcy.

Even in the event that a manager experienced a substantial reputational or operational event that called into question its ability to continue managing client assets, this is unlikely to result in a chaotic transition for client assets. As mentioned above, Appendix A highlights several examples of severe reputational issues at the adviser that resulted in the ultimate transition or winding down of the adviser or its funds. Appendix A also describes situations having similar results caused by distress at the adviser's parent company. Even in these severe situations, in some cases occurring during stressed markets, there were indications that a transition was becoming more likely and the transitions themselves did not occur suddenly without notice.

In order to understand this phenomenon, it is important to examine the governance structure of the asset owners. Most institutional investors have some combination of an investment committee, an investment consultant, a board or other oversight group. The process to terminate a manager varies from client to client, but when a manager experiences an event (major personnel departure, regulatory issue, change of control, etc.), many clients and consultants will put that manager "on watch" and some clients will immediately undertake a "review." This is a thoughtful process and clients seldom make a sudden knee-jerk decision. Further, different clients will often come to different conclusions. Additionally, even for clients who decide to change managers, the implementation of that change may require time. For example, a typical defined contribution plan offering a mutual fund will need time for the record-keeper to remove one fund and plug in another fund. In addition to the administrative aspects at the record-keeper, the plan sponsor will want to notify participants. All of this takes time, and throughout the process there is communication between the client and the manager. As a result, a manager is unlikely to get "surprise" or unexpected redemptions suddenly.

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[20] *Supra* note 8.

[21] See Appendix A for explanations of transitions relating to Bill Gross's departure from PIMCO and for findings of fraud and the violation of fiduciary duties from Strong Capital Management and Pilgrim Baxter & Associates.

Moreover, if an adviser is winding down and clients are transitioning to a new adviser, transaction costs will disincentivize clients from abruptly liquidating positions; they are often better off maintaining positions until they can re-establish them or change strategies with a new adviser. Thus, client transitions, even during a potential adviser insolvency could act counter-cyclically.

A Principles Based Approach is Required Given the Diversity of Adviser Business Models

Investment adviser business models are not homogeneous. We believe that a principles-based approach to transition planning is necessary to ensure that the Proposal is relevant for a broad range of investment advisers.

Investment advisers come in many shapes and sizes differing along multiple dimensions across the industry.[22] Areas where the business model of an investment adviser can differ widely include the capital structure of the parent company and affiliates, the asset class and product type focus, and the composition of the client base of the adviser. Transition planning needs to take into account the characteristics of the asset manager's business model and consider potential risk factors associated with that business model. Factors to consider in this regard include: (i) intrinsic revenue stability, (ii) level of leverage or exposure to debt, (iii) ability to adjust expenses using variable compensation to allow significant decreases in revenue to be offset by decreases in expenses, (iv) the type and diversity of asset classes (e.g., equity, fixed income, cash, real estate, private equity, emerging markets, etc.), (v) the type and diversity of investment processes (e.g., active, passive, quantitative, fundamental, etc.), (vi) the diversity of the clients (i.e., retail, institutional, insurance, etc.), (vii) the number and diversity of the products (e.g., separate accounts, mutual funds, ETFs, alternative funds, etc.), and additional affiliated products and services (e.g., custody, valuation, recordkeeping, technology platforms, etc.). Unlike a bank, where complexity is considered an indicator of risk, in the case of an asset manager, business diversity generally improves the stability of an asset manager's revenues and is, therefore, an indication of the resilience of the firm to withstand changes in client preferences and other short-term trends that might be damaging to concentrated, single strategy businesses. In fact, smaller firms with fewer resources present key man and succession planning issues, and single product firms present business concentration risk issues.

Advisers also differ in how they manage their balance sheets. This includes the extent of debt, how well cash is managed, intrinsic revenue stability, income statement resilience, and the consistency of the operating margin. In addition, an adviser may be impacted by whether its own or the adviser's parent company's balance sheet is highly leveraged and/or reliant upon short term funding to maintain day-to-day operations.[23] Some advisers have a diverse range of clients paying regular fees, an unlevered balance sheet that is not reliant on short-term funding, access to borrowing either from a parent entity or a bank, and the maintenance of stable operating income; as such an adviser is unlikely to suddenly go out of business. A lack of resilience in these areas would signal that a transition plan is more necessary. Even when financial stress

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[22] Office of Financial Research, Asset Management and Financial Stability, 3 (Sep. 2013), available at https://www.treasury.gov/initiatives/ofr/research/Documents/OFR_AMFS_FINAL.pdf.

[23] We do not believe this would be the case for the vast majority of advisers; however, to the extent this were the case for an adviser, it should be taken into account.

occurs, the strength and resilience of an adviser's business model determines how it will withstand that financial distress. Consequently, financial distress alone does not imply, by any means, that a transition is imminent.

As noted above, any risks associated with the transitioning of an adviser is mitigated by the fact that the assets themselves reside at a custodian, an entity that is legally separate from the adviser (even when the custodian and the adviser are affiliates). This affords the client protection in case of a disruption to the business of the adviser. With respect to information about the client's accounts, the ecosystem and common practice has developed to include multiple checks and balances and associated copies of the portfolio data. Independent copies of the portfolio and prices of securities often lie with an independent administrator.

In reviewing the Proposal in the context of the above described realities of the adviser business model, we think it is important to recognize that some of the requirements in the Proposal have been borrowed from a banking context and, therefore, they are not appropriate for transition planning for an asset manager. Specifically, advisers do not generally use their balance sheets to bail out their funds and often have very few assets on their balance sheets. They also do not engage in the types and extent of borrowing that banks do. The balance sheet of an asset manager generally comprises working capital, office space, corporate technology and goodwill, thereby requiring a modest amount of capital. An asset manager's balance sheet is typically very small compared with that of a bank or broker-dealer and its balance sheet generally is not leveraged significantly. Because the business of asset management is not capital intensive, asset managers do not routinely use short-term debt instruments to fund their operations and, thus, unlike banks and broker-dealers, asset managers are not dependent on continued liquidity from short-term markets. Given the context of the business models of advisers, we explain below specifically how each of the requirements of the transition plan could be adapted to reflect asset management activities.

<u>Policies and procedures intended to safeguard, transfer, and/or distribute client assets during transition:</u>

As we described above under "Contractual Provisions," mechanisms are already in place to safeguard client assets. In fact, this is a specific responsibility of the custodian. Unlike a bank, where client deposits are used in the business and are therefore at risk, the assets managed by asset managers are clearly separate from the balance sheet of the manager.

The Proposal also contemplates the transition of derivative positions. Unlike a bank whose balance sheet is exposed, asset managers are not the counterparty to client derivatives exposures. Further, while the standard transition management practice for derivatives instruments is for the legacy manager to close positions and the new manager to open desired positions, this is not the only option. For liquid and transparent derivatives, closing out derivatives positions provides clients with the ability to economically move positions among managers quickly and efficiently with minimal cost and risk. However, closing positions, if not desired by the client, is not entirely necessary since the client is the counterparty to derivatives transactions. The recent experience when Bill Gross suddenly left Pacific Investment Management Company ("PIMCO") was instructive in this regard. In our experience with separate accounts that were transferred from PIMCO to BlackRock, all over-the-counter derivatives positions were unwound by PIMCO during this time period for cash in an orderly way and re-executed by BlackRock, where necessary, and in line with the investment strategy to which we agreed with the client.

Policies and procedures facilitating the prompt generation of any client-specific information necessary to transition each client account:

We agree that it could be helpful for advisers to outline in their transition plans a mechanism that would facilitate the prompt retrieval of client contact information, to the extent practicable,[24] along with the contact information for counterparties, service providers, fund boards, and the like. In this regard, contact information, such as client and service provider contacts, as well as that of counterparties, that is already held for BCM purposes would be useful for transition purposes. Most of the information required for a transition, however, is also held at the record-keeper (e.g., for defined contribution plans), fund administrator, and custodian. Nonetheless, it could be helpful for advisers to maintain such a database in the event that it is required.

Information regarding the corporate governance structure of the adviser:

We agree that the corporate governance structure of a firm should be identified in a transition plan. The Commission also asks advisers to identify affiliates "whose dissolution or distress could lead to a change in or material impact to the adviser's business operations."[25] In this regard, it is important to remember that while there may be operational dependencies on affiliates that provide services to the adviser, this is not the same as a financial dependency. In other words, the financial distress of an affiliate does not necessarily translate into the financial distress of the adviser because advisers do not rely on short-term funding to fund their operations. Rather, the business model of investment advisers is revenue-driven, and when revenues decline, the adviser will eventually go out of business. The revenue stream does not disappear simply because an affiliate experiences distress. As such, we do not believe that it would be helpful or relevant for this issue to be addressed in adviser transition plans.

Identification of any material financial resources available to the adviser:

The Proposal states that "it is important for an adviser to have considered in advance its strategy for either avoiding or facilitating a transition of its business" and highlights that the adviser should identify financial resources that "it would seek in times of stress in order to continue operating or consider how it would implement a reduction of expenses or other alternatives."[26]

Asset managers often have the ability to significantly reduce expenses by reducing variable compensation in the event of revenue declines. In addition, asset managers can keep unencumbered cash on their balance sheets and they can have access to additional cash using letters of credit. Any assessment beyond the

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24 Advisers will have contact information for clients with whom they work directly, e.g., institutional clients. They will likely not have contact information for retail clients who may purchase products through intermediaries and cannot be expected to maintain this information as part of transition planning.

25 Proposal at 43524.

26 *Id.* at 43543.

identification of such fundamental resources should not be required. Since client assets are not on the balance sheet of the adviser, it is unclear what additional resources would be necessary to transition its business in times of stress.

An assessment of the applicable law and contractual obligations governing the adviser and its clients, including pooled investment vehicles, implicated by the adviser's transition:

We believe that the focus of this requirement should be funds, and not separate accounts. This is because separate account clients can terminate advisers at any time, making a change of control straightforward, and are expected to retain copies of their contracts.[27] Thus, this requirement should not apply to separate accounts, but only to funds. For funds, we support the concept of advisers having a mechanism in place to promptly access and retrieve fund constituent documents. Regarding the applicable law aspect of this requirement, we interpret this requirement to relate to identifying the type of contract, e.g., registered fund, private fund, etc. and the domicile of that fund, e.g., Delaware or The Cayman Islands for a private fund.

We do not believe that a further assessment of applicable law is necessary for advisers during the ordinary course of their business. Fund contracts already provide for or are governed by provisions that allow for an orderly transition. Specifically, registered funds are governed by the 1940 Act, and a fund board can act on behalf of shareholders as discussed above to hire a new adviser. With respect to private funds, both closed- and open-end, that are organized as limited partnerships, the partnership law in the most commonly used jurisdictions (including Delaware and the Cayman Islands) provides that a general partner is automatically removed as general partner of a limited partnership upon its insolvency or bankruptcy, and partnership agreements generally provide that in the event of such an insolvency or bankruptcy, the investors in that fund may either replace the general partner or cause the partnership to dissolve and be liquidated. With respect to changes of control, such as a "key person" event, the partnership agreement may include notice to the investors and remedies, including the right to remove and/or replace the general partner and the adviser. For the vast majority of private funds, the adviser to and general partner of a fund are separate, affiliated legal entities controlled by the same persons. With respect to private funds, again both closed- and open-end, that are organized in a form other than a partnership, such as a corporation, the board will typically have the ability to terminate the IMA between the fund and the adviser in enumerated circumstances, which typically include insolvency, bankruptcy, and/or a change of control with respect to the adviser.

Notice to the Commission

Transition plan documents should not be made public or filed with the Commission. These documents should be kept confidential as they often contain information, such as succession plans, which may not even be widely known within the adviser organization. Moreover, filing will make them more difficult to amend as circumstances change.

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27 For instance, for separate account clients subject to ERISA, termination cannot be penalized. "No contract or arrangement is reasonable within the meaning of section 408(b)(2) of the Act and paragraph (a)(2) of this section if it does not permit termination by the plan without penalty to the plan on reasonably short notice under the circumstances to prevent the plan from becoming locked into an arrangement that has become disadvantageous." 29 CFR 2550.408b–2(c).

That said, in the event the management of a significant proportion of the adviser's funds were transferred to another adviser, the Commission should be notified.

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III. Books and Records Rule: Comments on Amendments to Rule 204-2

Under the Proposal, the Commission would require each registered investment adviser to maintain copies of any business continuity and transition plan that is currently in effect, or that has been in effect during the past five years. Investment advisers would also have to maintain for five years all records documenting their annual reviews of their business continuity and transition plans. For the first two years of such period, these records would have to be maintained on-site in the investment adviser's offices.

BCM programs are updated annually and annual reviews are good business practice. They are also part of the annual review of compliance procedures required under Rule 206(4)-7. We believe that a record indicating that the relevant individuals approved updated policies and procedures during the last year should be a sufficient record of the annual review. The changes to the BCM program themselves should be reflected in new policies and procedures and no further record of changes to the program should be required. We believe that retaining old BCM programs and records of changes to programs is not necessary nor helpful to the Commission's oversight role. In any examination, the staff can confirm that the annual review occurred (by the record of such review by the responsible employees) and that the BCM program at the time of the examination meets the principles of the rule. The regulatory interest is whether at the time the appropriate plans are in place; a record of changes is superfluous. Thus, we recommend that the Commission eliminate its proposed requirement to keep these particular books and records for five years as such a requirement serves no regulatory purpose.

Further, the Commission requests comment on whether BCM programs should be filed with the Commission and if they should be made public.[28] We do not believe it is useful for regulators if almost 12,000 registered advisers each file BCM policies and procedures with the Commission,[29] many of which will number in the hundreds if not thousands of pages. We note that we know of no precedent for this type of filing. In addition, such filing requirements would make amending these policies more cumbersome and could incent advisers to update only annually, instead of being responsive to significant changes that could occur between annual reviews.

We strongly urge the Commission not to make details on these programs public for two reasons: (i) they contain details about a firm's business operations that could be used to support illicit behaviors, such as cyber-crime and (ii) they contain PII of the firm's employees.

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[28] Proposal at 43544.

[29] Investment Adviser Association, 2016 Evolution Revolution: A Profile of the Investment Adviser Profession, 8 (2016), available at http://www.nrs-inc.com/Global/Marketing%20Materials/Evolution%20Revolution%202016_v9.pdf.

We thank the Commission for providing BlackRock the opportunity to express our support for your efforts and to provide our comments and suggestions on the Proposal. Please contact the undersigned if you have any questions or comments regarding BlackRock's views.

Sincerely,

Barbara Novick
Vice Chairman

cc:

The Honorable Mary Jo White
Chairman
Securities and Exchange Commission

The Honorable Michael Piwowar
Commissioner
Securities and Exchange Commission

The Honorable Kara M. Stein
Commissioner
Securities and Exchange Commission

David Grim
Director
Division of Investment Management
Securities and Exchange Commission

Appendix A: Historical Examples of Adviser Transitions

SAC Capital Advisors, L.P

SAC Capital Advisors, L.P. ("SAC") was a Connecticut-based investment adviser started by Steven A. Cohen in 1992. SAC, along with certain other SAC entities, advised multiple hedge funds and managed approximately $16.5 billion in net assets at its peak in 2007. According to one media source, SAC "typically traded in stocks around market-moving events like earnings and big mergers."[30] In 2010, the SEC opened an insider trading investigation of SAC. According to media reports, in 2013, several of SAC's clients, including Citigroup Inc.'s private bank and Societe Generale's asset management unit, started exiting, pulling $1.68 billion as several former employees of SAC were indicted by the US Department of Justice. In November 2013, the firm itself plead guilty to insider trading charges and paid $1.8 billion in penalties and shut down its investment-advisory business.[31] The firm returned the vast majority of its outside investor capital and shrunk significantly in terms of number of employees and assets under management ("AUM"). In 2014, within one year of SAC pleading guilty to insider trading charges, Cohen founded Point72 Asset Management ("Point72") as a separate family office to become the successor to SAC. SAC transferred the bulk of its assets to Point72 in 2014, resulting in a Point72 AUM of $11 billion as of 2015. SAC still exists as a separate entity as of early 2016, and is winding down all operations.

Bear Stearns

Bear Stearns was the fifth largest investment bank in the US prior to its acquisition by JPMorgan Chase. It engaged primarily in capital market activities, including underwriting, trading and dealing in equities, bonds and derivatives; wealth management; and the provision of global clearing services. Through a subsidiary, Bear Stearns was the sponsor of two structured credit funds that were almost entirely invested in thinly traded complex derivatives backed by subprime mortgages. Both funds were highly leveraged. When the subprime mortgage market faltered, these funds suffered large losses and were unable to meet investor redemptions or margin calls against falling collateral values. In June 2007, Bear Stearns made a collateralized loan to one fund, and in April 2007 a $25 million investment in the other fund.[32] In July 2007, both funds lost nearly all their value and were placed into bankruptcy. Bear Stearns had no legal obligation to bail out either fund, and it did not do so. When these funds went bankrupt, the vast majority of the losses were taken by investors in the funds and the funds' lenders and not by Bear Stearns itself. As a result of the continued decline in the value of mortgage-backed securities, in mid-March 2008, the US Government arranged support for JPMorgan Chase to acquire Bear Stearns, with JPMorgan Chase ultimately paying $10 per share for Bear Stearns equity. Importantly, this acquisition was eight months after the structured credit funds were put into liquidation, and no government support was provided to the funds.

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[30] Peter Lattman and Ben Process, New York Times, *$1.2 Billion Fine for Hedge Fund SAC Capital in Insider Case* (Nov. 4, 2013), available at http://dealbook.nytimes.com/2013/11/04/sac-capital-agrees-to-plead-guilty-to-insider-trading/.

[31] Saijel Kishan, Bloomberg, *Cohen-SAC Timeline: Firm's Guilty Plea End Criminal Case* (Nov. 4, 2013), available at http://www.bloomberg.com/news/articles/2013-11-04/cohen-sac-timeline-firm-s-guilty-plea-end-criminal-case.

[32] Financial Crisis Inquiry Commission, *The Financial Crisis Inquiry Report: Final Report of the National Commission on the Causes of the Financial and Economic Crisis in the United States*, 240-41 (2011).

Neuberger Berman Asset Management

One of the subsidiaries of Lehman Brothers Holdings ("Lehman") was Neuberger Berman Asset Management ("Neuberger Berman"), which did not enter bankruptcy with its parent. Lehman sold Neuberger Berman to Neuberger Berman's management (with the Lehman bankruptcy estate retaining an equity interest) in a bankruptcy auction in December 2008.[33] Neuberger Berman purchased the Lehman estate's equity interests in 2012, and operates as a successful stand-alone asset manager today.[34]

PIMCO

While not an adviser transition, the recent outflows from PIMCO Total Return Strategy funds following the resignation announcement of lead portfolio manager Bill Gross in September 2014 provides an example of a significant reputational event and its effect on client assets in 2014-2015. It demonstrates the ability to transition large amounts of assets from one manager to another without market disruption and the existence of a large number of competitors in the industry. Outflows from PIMCO funds were primarily observed in products most closely associated with Bill Gross as the portfolio manager. October 2014 outflows from PIMCO totaled $48 billion, 70% of which came from funds previously managed by Gross.[35] Likewise, the PIMCO Total Return Fund saw overall outflows of $68 billion from October 2014 through January 2015, with larger outflows in both January 2015 and December 2014 than in November 2014.[36] While specific attribution of the aggregate outflows to receiving funds is difficult to ascertain, public data show that the flows were spread across multiple firms, products, and investment strategies, reflecting a high level of competition in the asset management industry.[37] Various asset owners chose between active, passive, and unconstrained strategies offered by more than a half-dozen asset managers; the data indicate that some clients may have bought shares in fixed income ETFs. Despite these movements, fixed income markets, including related derivative instruments, continued to function in an orderly manner during this period of relatively low market liquidity.

33 DealBook, New York Times, *Lehman's Neuberger Sale Is Approved* (Dec. 23, 2008), available at http://dealbook.nytimes.com/2008/12/23/lehmans-neuberger-sale-is-approved/?_r=1.

34 Neuberger Berman, *Neuberger Berman Outperforms Over 10 Year Period and Wins New Business; Moves Toward 100% Employee Ownership* (June 5, 2012), available at https://www.nb.com/press_center/.

35 Kirsten Grind, The Wall Street Journal, *Pimco Sees $48 Billion in Outflows After Gross Departure* (Nov. 5, 2014), available at http://www.marketwatch.com/story/pimco-sees-48-billion-in-outflows-after-gross-departure-2014-11-05. Oliver Suess, Bloomberg, *Pimco Offers Special Post-Gross Bonus to Retain Talent* (Nov. 7, 2014), available at http://www.bloomberg.com/news/articles/2014-11-07/pimco-offers-special-post-gross-bonus-to-retain-talent.

36 PIMCO Press Releases, available at http://www.pimco.com/en/pressreleases/Pages/PressReleasesOverview.aspx.

37 Jackie Noblett, Ignites, *Schadenfreude: Shops That Gained Most From Pimco's Pain* (Sep. 25, 2015), available at

http://www.ignites.com/c/1205373/132563/schadenfreude_shops_that_gained_most_from_pimco_pain?

Strong Capital Management and Pilgrim Baxter & Associates

In 2004, two advisers went out of business at the same time. Each adviser was able to fully transition its business in less than one year, without having any material impact on the market.

The chief executive and founder of Strong Capital Management ("Strong Capital") was implicated in facilitating market timing abuses in September 2003, at which time Strong Capital managed approximately $42 billion in client accounts. Because of the severe reputational damage caused to Strong Capital as a result of this issue, the funds managed by Strong Capital were acquired by Wells Fargo in 2004. Through this transaction, Strong Capital's funds were reorganized into the Wells Fargo Funds® family. The legal entities comprising the Strong Financial complex were subsequently liquidated. To our knowledge, there was no market impact or forced asset liquidations as a result of the circumstances.

Pilgrim Baxter & Associates ("Pilgrim Baxter"), manager of the PBHG fund family, suffered severe reputational damage at the end of 2003 when principals Gary Pilgrim and Harold Baxter were accused of fraud and breach of fiduciary duty for allowing market timing abuses in the funds they managed. As a result of the reputational damage from the scandal, PBHG funds lost more than one-third of their AUM in one year. The PBHG funds were rebranded under the name of Pilgrim Baxter parent company, Old Mutual, in 2004, and Pilgrim Baxter changed its name to Liberty Ridge Capital. To our knowledge, these events did not have a material market impact.

BlueCrest Capital Management

BlueCrest Capital Management ("BlueCrest") was an investment adviser established in 2000 by Michael Platt and based in New Jersey. In 2012, BlueCrest managed around $36 billion in AUM across a range of funds, including equity, credit, and emerging market portfolios.[38] In December 2015, with $8 billion in AUM, BlueCrest announced that it would stop managing money for outside clients and manage money only for its partners and employees, converting the firm into a private investment partnership.[39] This move followed a significant drop in AUM and poor returns from the firm's flagship fund, BlueCrest Capital International, including the New Jersey State Investment Council withdrawing about $284 million from BlueCrest due to disappointing results. According to press reports, consultants Albourne Partners and Aksia reported a lack of transparency to external investors at BlueCrest in 2014, and subsequently the Orange County Employees Retirement System withdrew its BlueCrest investment. As part of the motivation for the transition, BlueCrest executives noted that their client base had become increasingly focused on levels of risk and lower levels of fees.[40] In its transition to a private partnership platform, BlueCrest is expected to close most of its funds, including BlueCrest Capital International and the AllBlue fund, while a few funds

38 Laurence Fletcher, The Wall Street Journal, *Hedge Fund BlueCrest Capital to Return Outside Clients' Money* (Dec. 1, 2015), available at http://www.wsj.com/articles/hedge-fund-bluecrest-capital-to-return-outside-clients-money-1448976411.

39 Alexandra Stevenson and Matthew Goldstein, The New York Times, *BlueCrest to Close Hedge Fund and Refund Outside Investors* (Dec. 1, 2015), available at http://www.nytimes.com/2015/12/02/business/dealbook/bluecrest-capital-to-return-money-to-outside-investors.html?_r=0.

40 Miles Johnson, The Financial Times, *BlueCrest's own partners' fund fares better than clients'* (Dec. 18, 2015), available at http://www.ft.com/cms/s/0/4eb275f2-a4dd-11e5-a91e-162b86790c58.html#axzz4Iju261MO.

will be retained as vehicles for partners and employees to invest.[41] BlueCrest is expected to return all external client money by the end of 2016, and media reports as of June 2016 state that BlueCrest has already returned $7 billion.[42]

41 PRNewswire, *BlueCrest Capital Management to Become Private Investment Partnership* (Dec. 1, 2015), available at http://www.prnewswire.com/news-releases/bluecrest-capital-management-to-become-private-investment-partnership-559485421.html.

42 Kerry Close, Time, *More Hedge Funds Closed Over the Past Year Than* Opened (Jun. 16, 2016), available at http://time.com/money/4371669/hedge-funds-closing/.