ES155012

United States Senate

WASHINGTON, DC 20510

November 29, 2016

Hon. Mary Jo White
Chair
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549

Dear Chair White:

We are writing regarding proposed Rule 18f-4 under the Investment Company Act of 1940, which addresses the use of derivatives by Registered Investment Companies and Business Development Companies. We applaud the Commission for tackling the complex issues raised by mutual funds that use derivatives and for undertaking an effort to consolidate into a single, uniform rule the previous formal and informal guidance about how mutual funds should and should not trade in derivatives. We are particularly pleased that the proposed rule defines risk management oversight. At the same time, we urge the Commission to consider all the potential unintended side effects of its proposal to ensure that investors are able to continue to diversify their portfolios fully and, as a result, manage the risks of various asset classes.

The use of speculative derivatives played a significant role in sparking the financial crisis of 2008, which contributed to serious economic harm to the public and destroyed confidence in the financial system. One of the most important reforms to arise out of the crisis was, therefore, more robust oversight of derivatives trading and central clearing requirements, and we remain strongly supportive of appropriately tailored derivatives oversight as it relates to usage by mutual fund investments.

At the same time, derivatives have an important role to play in managing risk and promoting diversification, often across asset classes. Many mutual funds employ strategies that use simple derivatives on low risk assets, including government bonds, interest rates, and currencies. Investing in these funds allows investors to diversify their risk away from an over-concentration in one asset class. A rule that would prevent risk mitigation or diversification into these lower risk assets or strategies could actually harm investors by forcing them to assume even more risk.

As you continue to refine the proposal, we respectfully urge you to maintain the ability of investors to diversify their portfolios to guard against excessive swings in the stock market and other risks. Therefore, it is important that the rule distinguish between the complex derivatives that hide risks or derivatives that create very high and inappropriate levels of risk and simple derivatives that facilitate investor diversification or derivatives that do not create excessive risk and facilitate investor exposure to low risk underlying assets.

Thank you for considering our views.

Sincerely,

Mark R Warner

Mark Warner
U.S. Senator

Joe Donnelly

Joe Donnelly
U.S. Senator

Heidi Heitkamp

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U.S. Senator

cc: Commissioner Michael Piwowar
Commissioner Kara Stein