William Blair

March 28, 2016

VIA EMAIL

Mr. Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Use of Derivatives by Registered Investment Companies and Business Development **Companies; Release No. IC-31933; File No. S7-24-15**

Dear Mr. Fields:

We appreciate the opportunity to comment on the Securities and Exchange Commission's (the "SEC's") above-referenced proposal regarding the use of derivatives by registered investment companies and business development companies (the "Proposal.") William Blair & Company, L.L.C. was founded more than 80 years ago and registered as an investment adviser in 1947. Together with its registered investment adviser affiliate, William Blair Investment Management, LLC, (collectively, "William Blair"), William Blair manages approximately $65 billion in regulatory assets under management. William Blair Investment Management, LLC currently advises 24 mutual funds, each of which is organized as a separate series within a single Delaware statutory Trust (the "William Blair Funds") and one mutual fund that is a series of the Trust for Professional Managers (collectively with the William Blair Funds, the "Funds"). As of December 31, 2015, the Funds had approximately $14 billion in assets.

We support the SEC's efforts to modernize the regulation of derivatives and safeguard investors and our financial system. In particular, the Proposal's requirements regarding asset segregation for derivatives transactions coupled with a derivatives risk management program, for affected funds, together address many of the SEC's concerns regarding derivatives usage within retail funds. As noted by Commissioner Piwowar, "[t]he proposed asset segregation requirements should function as a leverage limit on funds and ensure that funds have the ability to meet their obligations arising from derivatives."[1] We concur with Commissioner Piwowar: requiring funds to segregate qualifying coverage assets[2] equal to the mark-to-market coverage amount (the amount that the fund would be required to pay if it exited the derivatives transaction at the time determined) plus the risk-based coverage amount (the amount representing a reasonable estimate of the potential amount the fund would pay if it exited the derivatives transaction under stressed conditions) acts as a de facto limit on the overall derivatives exposure a fund could incur. In addition, establishing a formalized derivatives risk management program, led by an independent, prudent derivatives risk manager that is not a portfolio manager, is an additional measure designed to manage the particular risks presented by derivatives usage that is consistent with a fund's investment objectives and restrictions, risk profile, policies and relevant regulatory requirements. We believe this combination would provide sufficient safeguards to protect

[1] Dissenting Statement at Open Meeting on this Proposal (December 11, 2015).
[2] Please see our comments with respect to Asset Segregation/Qualifying Coverage Assets below.

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investors. The Proposal's added portfolio limitations for derivatives transactions either under the Exposure-Based Portfolio Limit (the "Notional Test") or Risk-Based Portfolio Limit (Value at Risk or the "VaR Test") are unnecessary, overly complex and, as proposed, do not provide a meaningful measurement of the risk or leverage of a portfolio.

However, should the SEC require funds to comply with portfolio constraints beyond sound asset segregation; we encourage the SEC to consider alternatives in formulating both the Notional Test and VaR Test,[3] each providing a more meaningful assessment of a fund's derivatives exposure. First, with respect to the Notional Test, we suggest that the SEC amend the Proposal to recognize a "risk weighting" for each of the underlying derivatives transactions before calculating the fund's notional exposure. Second, we suggest that the SEC replace its proposed VaR Test with the following: the overall value at risk ("VaR") of a fund's portfolio may not exceed 1.5 times the VaR of an identified global equity benchmark ("1.5xVaR Test"). Our suggested modifications to the proposed Notional Test and VaR Test are not conditional or mutually exclusive and can be viewed independently.

Exposure-Based Portfolio Limit/Notional Test

The SEC's Division of Economic and Risk Analysis White Paper (the "White Paper") states that there are "drawbacks to using notional amounts... because of the differences in expected volatilities of the underlying assets, notional amounts of derivatives across different underlying asset[s] generally do not represent the same unit of risk."[4] The White Paper sets forth the following example: "the level of risk associated with a $100 million notional of a S&P500 index futures is not equivalent to the level of risk of a $100 million notional of interest rate swaps, currency forwards or commodity futures."[5] In its Proposal, the SEC recognizes that the Notional Test could be viewed as a "relatively blunt measurement in that different derivatives transactions having the same notional amount but different underlying reference assets...may expose a fund to very different potential investment risks and potential payment obligations."[6] However, the Proposal sets forth the argument that, on balance, the use of a notional amount limitation, measured immediately after entering into any such senior securities transaction (derivatives transactions, financial commitment transactions and other transactions involving a senior security) would be a more effective and administrable means of limiting potential leverage from derivatives than a limitation relying on other leverage measures. We respectfully disagree with this approach.

We recommend that the SEC apply its proposed Notional Test to the sum of the risk-weighted notional exposure of each derivative transaction instead of to the sum of the notional exposure of each unweighted derivative transaction. This approach recognizes the differences in risk among classes of derivatives by using a weighting mechanism (either up or down). We further recommend that the SEC adopt standardized risk weights recognizing that some derivatives transactions are inherently less risky when aggregating the total notional exposure of a fund's portfolio.

[3] We understand that the Investment Company Institute and other industry participants are submitting comments with respect to increasing the overall exposure limits.

[4] Use of Derivatives by Registered Investment Companies, Daniel Deli, Paul Hanouna, Christof W. Stahel, Yue Tang and William Yost, Division of Economic and Risk Analysis (December 2015), Section 7.1 at page 10.

[5] Id.

[6] Proposal at 70.

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In connection with international, risk-based and leverage capital requirements for bank-type financial institutions, other financial regulators, including U.S. prudential regulators, adopted a Standardized Approach for Risk-Weighted Assets.[7] When setting capital requirements for banking institutions, these bank regulators use safety and soundness principles in analyzing assets on the books of the institution. While the SEC's mission to protect investors and to maintain fair, orderly and efficient markets differs somewhat from the bank regulators' missions to maintain stability and public confidence in the nation's financial system, a standardized, risk-weighted table would provide all funds with clear guidelines.

To illustrate, we recommend, as an example, that the SEC apply a set of risk weights that are derived from the factors specified by the Federal Deposit Insurance Corporation ("FDIC") in determining the risk-based capital requirements for over-the-counter ("OTC") derivative contracts.[8] Specifically, the risk weight percentages for each class of derivative is calculated as the FDIC credit conversion factor for that class divided by the FDIC credit conversion factor for equity derivatives greater than five years. Using this calculation essentially normalizes each class of derivative to equities. The risk weight for interest rate derivatives with one year or less remaining maturity can be set equal to the risk weight for foreign exchange instruments with one year or less of remaining maturity, thereby avoiding a risk weight of zero that the FDIC table would otherwise suggest. The resulting table of risk weights is as follows:

Remaining Maturity	Interest Rate	FX and Gold	Credit IG	Credit Non-IG	Equity	Precious Metals	Other
One year or less	10%	10%	50%	100%	60%	70%	100%
Between 1 year and five years	10%	50%	50%	100%	80%	70%	120%
Greater than five years	15%	75%	50%	100%	100%	80%	150%

[7] For example, see Federal Deposit Insurance Corporation Regulatory Capital Rules: Regulatory Capital, Implementation of Basel III, Capital Adequacy, Transition Provisions, Prompt Corrective Action, Standardized Approach for Risk-weighted Assets, Market Discipline and Disclosure Requirements, Advanced Approaches Risk-Based Capital Rule, and Market Risk Capital Rule: Federal Register, Vol. 78, No. 175 (September 10, 2013). See also, Board of Governors of the Federal Reserve System and the Office of the Comptroller of the Currency.

[8] See Appendix A for a copy of Section L of "Regulatory Capital Rules: Standardized Approach for Risk-Weighted Assets; Market Discipline and Disclosure Requirements." Financial Institution Letter FIL-27-2012, p.10 (June 18, 2012).

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Using this set of risk weights, and the table of instruments contained on page 69 of the Proposal, the following is an example of how risk weights would be applied.

Position Type	Example	Notional under Proposal	Risk weight	Risk-Weighted Adjusted Notional
FX forward	3 month $10 million USD vs. EUR	$10 million	10%	$1 million
FRA	1 month into 1 year $10 million	$10 million	10%	$1 million
Treasury Futures	100 30 year Bond Futures	$13.77 million	15%	$2.07 million
Interest Rate Futures	10 Eurodollar Futures	$10 million	10%	$1 million
FX Futures	10 JPY/USD Futures	125 million JPY=$1.093 million USD	10%	12.5 million JPY=$109.3 thousand USD
Equity Index Futures	100 S&P 500 eMini Futures	$9.65 million	60%	$5.79 million
Commodity Futures	100 crude oil Futures	$3.39 million	100%	$3.39 million
Options on Futures	100 at the money 2 year S&P 500 eMini call options (50 delta)	$4.83 million	80%	$3.86 million
Credit Default Swap	10 million notional of 7 year CDX high yield	$10 million	100%	$10 million
Standard Total Return Swap	50,000 units of 5 year TR5 on S&P GSCI Excess Return CME index, a broad commodity index	$10 million	150%	$15 million
Currency swap	$10 million 2 year swap USD vs. GBP	$10 million	50%	$5 million
Cross currency interest rate swap	5 year swap on $10 million USD fixed vs. EUR floating	$10 million	75%	$7.5 million
Security Options	2000 ATM LEAPS on XLE (50 delta)	$5.7 million	80%	$4.46 million
Currency Options	$20 million 18 month 50 delta USD Call / EUR put	$10 million	50%	$5 million
Index Options	13 month $40 million 25 delta S&P 500 call	$10 million	80%	$8 million

As demonstrated by the table above, there is a wide range of risk-weights associated with underlying derivatives transactions from short dated FX Forwards to long-dated commodity swaps.

While we would favor a Notional Test that takes into account appropriate netting and off-setting transactions, we understand that administering a comprehensive set of rules may not be feasible. Therefore, we believe that calculations using standardized risk-weighting factors, as recommended above, would: (1) fairly reflect the notional exposure of each underlying derivatives transaction and the overall notional exposure of a fund's portfolio; (2) not be overly complicated; and (3) be relatively simple to administer. In addition, because funds with derivatives exposure would use the same adjusted risk weights in calculating their specific fund's notional exposure, the SEC should be able to compare derivatives risk exposure information across funds. In addition, such an approach would better assess relative risk than a simple notional approach. Lastly, we recommend that the SEC periodically review and update the risk weighting assigned to the classes of derivatives transactions reflected in the standardized table based on information in the marketplace and gathered from regulatory examinations and updated regulatory filings.

Risk-Based Portfolio Limit/VaR Test

With respect to the Proposal's alternative VaR Test, we believe that requiring the fund's full portfolio VaR to be less than the fund's securities VaR immediately after the fund enters into any senior securities transaction runs counter to how many funds use derivatives in order to meet their stated investment objectives. Not all derivatives transactions hedge or reduce risk. Derivatives transactions are commonly used to obtain efficient and cost-effective market exposure and may increase the fund's portfolio VaR. In addition, requiring the fund to run this complicated, time consuming analysis immediately after entering into each derivative transaction would effectively prohibit certain trades from occurring simultaneously in the market, such as spread trades, rolls or market on close trades.

Instead, we recommend that the alternative VaR Test be calculated once daily and be based on the overall VaR of a fund's portfolio in comparison to the VaR of an identified benchmark.[9] Currently, given that mutual funds with no derivatives exposure may borrow amounts that do not exceed 50% of its assets, excluding the amount of the borrowing, we recommend that the SEC replace its proposed VaR Test with the following alternative 1.5xVaR Test: the overall VaR of a fund may not exceed 150% of the VaR of a widely adopted, unlevered global equity benchmark. If the fund can meet this 1.5xVaR Test, the fund may increase its risk-weighted notional exposure of its derivatives and other senior securities transactions to any upper notional limit, as adopted. This approach appears to meet the objectives of the SEC under the Proposal: (1) it provides a metric to assess the effect of derivatives use on a fund's exposure to market risk;[10] and (2) it establishes a threshold on the overall VaR of the fund. In addition, this approach sets forth an objective measure against which all funds can be compared. As discussed previously in connection with a standardized, risk-weighting of assets underlying a Notional Test, utilizing a once daily comparison to a standard benchmark should be relatively straight-forward, administratively feasible and allow the SEC to compare derivatives exposure information across funds.[11]

[9] We understand that some industry participants are recommending, for purposes of the VaR Test, that the designated benchmark could vary from fund to fund as long as the VaR benchmark is disclosed in the fund's prospectus and statement of additional information.

[10] Proposal at 119.

[11] As noted by the SEC, some UCITS funds may use an absolute VaR approach which limits the maximum VaR that a UCITS fund can have relative to its net assets (generally at 20% of the UCITS fund's net assets). We believe that our

Asset Segregation/Qualifying Coverage Assets

As previously stated, we generally concur with the SEC's proposed two-pronged asset segregation approach with respect to derivatives transactions. However, we suggest that the SEC expand the type of assets considered as "qualifying coverage assets" under both the mark-to-market coverage and risk-based coverage amounts. The Proposal defines qualifying coverage assets to include cash and cash equivalents (certain Treasury bills, agency securities, bank deposits, commercial paper and shares of money market funds).[12] We recommend that the Proposal be expanded to include, as appropriate, all liquid securities as qualifying coverage assets. However, we suggest that for those liquid securities deemed riskier than cash or cash equivalents, a discount be applied similar to those adopted by banking regulators (for example, Margin Values for Eligible NonCash Margin Collateral for Covered Swap Entities).[13]

As with our other comments, we strongly believe that applying a standard model for determining qualifying coverage assets, especially when already widely used by the industry and other regulators, will further the SEC's objective for effective asset segregation. Utilizing standardized tables across the industry when a fund complex segregates qualified coverage assets reduces the likelihood that a fund will be unable to cover an outstanding derivatives transaction.

General Comments

If the SEC's Derivatives Rule is adopted as proposed, there may be a number of unintended consequences that follow: increased shareholder costs, potential loss of investment opportunity, cash drag on performance and potential diminished value of performance history. If there is no risk-weighted adjustment put in place for the Notional Test, portfolio managers wishing to hedge against currency risk may need to purchase dollar denominated equivalent securities with higher embedded costs than an FX derivative. Alternatively, a portfolio manager may decide not to hedge against the currency risk, thereby exposing the portfolio to potentially undesirable risks, including increased volatility. Similarly, portfolio managers seeking to capture differences in synthetic funding markets (relative to cash returns) can do so only by investing in derivatives transactions. By limiting a fund's ability to invest in derivatives transactions, in certain markets, there is a possibility that shareholders could experience lower potential returns because the opportunity to exploit differences in synthetic funding markets is no longer available at attractive rates.

If the definition of qualifying coverage assets is not expanded, portfolio managers will need to maintain more of a fund's assets in cash and cash equivalents to meet the asset segregation requirements for derivatives transactions thereby creating cash drag on a portfolio's performance. Exacerbating the potential cash drag issue, many funds invest excess cash in overnight cash products at their custodians (backed by overnight repurchase agreements on government securities). However, if

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alternative approach is a more effective way to use VaR to provide a risk assessment of a fund's use of derivatives than absolute VaR underlying the UCITS regime.

[12] Proposal at 179.

[13] See Appendix B for a copy of Table B from the "Margin and Capital Requirements for Covered Swap Entities" adopted by the Comptroller of the Currency, Federal Reserve Board, Federal Deposit Insurance Corporation, Federal Credit Administration and Federal Housing Finance Agency, Federal Register, 80 FR 74839 (November 30, 2015).

the Proposal deems standard "cash products" to be viewed as derivatives transactions, subject to exposure and risk-based limits, funds may need to invest excess cash in lower-yielding alternatives. Moreover, depending on the extent of cash and cash equivalents needed to meet the proposed asset segregation requirements, a fund may not be able to be managed as in the past and may diminish the value of an established track record.

As discussed throughout, we recommend that any final rule require the fund to conduct either the Notional Test or alternative VaR Test once daily. Running either test, but especially the alternative VaR Test, immediately after entering into each derivative transaction would be operationally difficult and inefficient. Common trading techniques such as spread trades, hedging trades and FX rolls that require near simultaneous execution of multiple derivatives transactions could all be impacted if an intervening VaR analysis had to be completed before the full trade is finalized. During this intervening period of time, market movement risk is introduced that may impact the portfolio and ultimately the shareholder. In addition, augmenting current reporting tools to provide for intra-day VaR testing would require systems development and a lengthy implementation process.

We recognize that the SEC is advancing this Proposal along with a number of other regulatory initiatives that will impact registered investment companies and their registered investment advisers. Specifically, the SEC has proposed rulemaking with respect to establishing liquidity risk management programs and swing pricing and modernizing and enhancing fund reporting. In addition, we understand that the SEC is considering new requirements for stress testing by large investment advisers and investment companies. We urge the SEC not to consider this Proposal in a vacuum and to analyze it in the context of all other pending proposals. Together, all of these proposed rules are meant to strengthen the fund industry, reduce risk to shareholders, modernize reporting and provide increased investor protection. Therefore, we recommend that the compliance date after adoption of any Final Rule for this Proposal be considered in conjunction with the implementation date, including any applicable phase in periods, for these related proposed rule-makings.

Many fund shareholders seek to diversify their overall portfolio by investing in products that offer lower correlation to long-only equity markets as well as to other mutual fund products. If funds are not able to fully utilize derivatives transactions, there will be a much higher correlation with the long-only equity market, in general, and between available funds. If adopted as proposed, a number of today's existing funds may be unable to operate in such a way as to meet their stated investment objectives and may be forced to close to retail investors. In addition, the elevated costs associated with the Proposal may be a barrier to entry for new managers. Together, the Proposal may have the effect of reducing the number of diversifying products available to retail investors, including those saving for retirement, who may otherwise be unable to invest in private funds due to accredited investor requirements, high investment minimums and fees and illiquidity. The Proposal's recommendations with respect to a derivatives risk management program and reasonable, discounted asset segregation coupled with the separately proposed changes to liquidity management and fund reporting and disclosure will sufficiently provide enhanced investor protection. In addition, if the SEC determines later that additional protection is warranted, it can at that time layer on new or revised conditions. Informed investors should be able to select funds that use derivatives transactions as long as those transactions meet the stated investment objectives and risk tolerance of the fund and assets are properly segregated.

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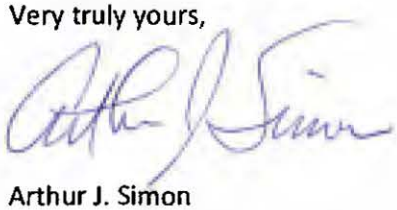
We appreciate the opportunity to comment on the Proposal. If you have any questions about our comments or would like any additional information, please contact me or Jeannette Lewis at (312) 236-1600.

Very truly yours,



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Appendix A[14]

The table below shows the credit conversion factors for derivative contracts:

Remaining Maturity	Interest Rate	Foreign Exchange Rate and gold	Credit (investment grade and reference asset)	Credit (non-investment grade reference asset)	Equity	Precious metals (except gold)	Other
One year or less	0.0 %	1.0%	5.0 %	10.0%	6.0%	7.0%	10.05
Greater than one year and less than or equal to five years	0.5%	5.0%	5.0%	10.0%	8.0%	7.0%	12.0%
Greater than five years	1.5%	7.5%	5.0%	10.0%	10.0%	8.0%	15.0%

[14] Section L of "Regulatory Capital Rules: Standardized approach for Risk-Weighted Assets; Market Discipline and Disclosure Requirements," adopted by the Federal Deposit Insurance Corporation, Financial Institution Letter FIL-27-2012, p. 10 (June 18, 2012).

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Appendix B[15]

Appendix B to [Part]—Margin Values for Eligible Noncash Margin Collateral.

TABLE B—MARGIN VALUES FOR ELIGIBLE NONCASH MARGIN COLLATERAL

Asset class	Discount (%)
Eligible government and related (e.g., central bank, multilateral development bank, GSE securities identified in §__.6(a)(2)(iv) or (b)(5) debt: residual maturity less than one-year	0.5
Eligible government and related (e.g., central bank, multilateral development bank, GSE securities identified in §__.6(a)(2)(iv) or (b)(5) debt: residual maturity between one and five years	2.0
Eligible government and related (e.g., central bank, multilateral development bank, GSE securities identified in §__.6(a)(2)(iv) or (b)(5) debt: residual maturity greater than five years	4.0
Eligible GSE debt securities not identified in §__.6(a)(2)(iv) or (b)(5): residual maturity less than one-year	1.0
Eligible GSE debt securities not identified in §__.6(a)(2)(iv) or (b)(5): residual maturity between one and five years:	4.0
Eligible GSE debt securities not identified in §__.6(a)(2)(iv) or (b)(5): residual maturity greater than five years:	8.0
Other eligible publicly traded debt: residual maturity less than one-year	1.0
Other eligible publicly traded debt: residual maturity between one and five years	4.0
Other eligible publicly traded debt: residual maturity greater than five years	8.0
Equities included in S&P 500 or related index	15.0
Equities included in S&P 1500 Composite or related index but not S&P 500 or related index	25.0
Gold	15.0

[1] The discount to be applied to an eligible investment fund is the weighted average discount on all assets within the eligible investment fund at the end of the prior month. The weights to be applied in the weighted average should be calculated as a fraction of the fund's total market value that is invested in each asset with a given discount amount. As an example, an eligible investment fund that is comprised solely of $100 of 91 day Treasury bills and $100 of 3 year US Treasury bonds would receive a discount of (100/200)*0.5+(100/200)*2.0=(0.5)*0.5+(0.5)*2.0=1.25 percent.

[15] Table B, "Margin and Capital Requirements for Covered Swap Entities," adopted by the Comptroller of the Currency, Federal Reserve Board, Federal Deposit Insurance Corporation, Federal Credit Administration and Federal Housing Finance Agency, 80 FR 74839 (November 30, 2015).