

December 23, 2022

Vanessa A. Countryman
Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

Via email: rule-comments@sec.gov

Re: Outsourcing by Investment Advisers (File No. S7-25-22)

Dear Ms. Countryman:

State Street Corporation¹, including its investment management arm, State Street Global Advisors, (collectively, “State Street”) appreciates the opportunity to respond to the Securities and Exchange Commission’s (the “Commission” or “SEC”) proposed rule regarding the implementation of new due diligence and oversight requirements for SEC-registered investment advisers (“RIAs”) relative to their outsourcing of certain financial services and functions to third party entities (“Proposal”).² While State Street recognizes the importance of RIAs conducting appropriate due diligence prior to hiring third parties to provide services with respect to the management of RIA client accounts, we do not believe that the proposed framework is appropriate or necessary, given the existing fiduciary duties, regulatory obligations and operational practices that today define the relationship between RIAs

¹ Headquartered in Boston, Massachusetts, State Street Corporation is a global custody bank which specializes in the provision of financial services to institutional investor clients. With \$35.688 trillion in assets under custody and administration and \$3.265 trillion in assets under management as of September 30, 2022, State Street operates in more than 100 geographic markets globally.

*AUM as of September 30, 2022 includes approximately \$55 billion of assets with respect to SPDR® products for which State Street Global Advisors Funds Distributors, LLC (SSGA FD) acts solely as the marketing agent. SSGA FD and State Street Global Advisors are affiliated.

² Available at <https://www.sec.gov/rules/proposed/2022/ia-6176.pdf>.

and the service providers they hire. As such, we urge the Commission to withdraw the Proposal in its entirety. If the Commission nonetheless chooses to move forward with the Proposal, we recommend that custody, fund administration and transfer agent services provided by bank custodians be explicitly excluded from the term “covered function”, as bank custodians already have robust risk management programs in place that comply with relevant regulatory and supervisory expectations for the proper conduct of their business activities.

EXISTING FIDUCIARY DUTIES SUFFICIENTLY ADDRESS THIRD PARTY VENDOR OVERSIGHT

State Street strongly urges that the Proposal, in its entirety, be withdrawn by the Commission because the Proposal as drafted, is inappropriately and overly prescriptive and, more importantly, it is unnecessary due to the fact that existing fiduciary duties owed by investment advisers with respect to the oversight of vendors already cover the concerns and issues the Proposal purportedly seeks to address. While the Commission acknowledges that RIAs are fiduciaries, and therefore subject to the obligation to place the interest of their clients ahead of their own, it fails to recognize the crucial role which this obligation places upon the adviser in the conduct of its oversight responsibilities. Indeed, fiduciary obligations are enforceable under existing regulations and cannot be discharged by the adviser. It is therefore prudent and a fundamental obligation of investment advisers already that they perform appropriate due diligence and continuous monitoring of activities outsourced to third party vendors, where such outsourcing has, or could have, a material impact on the level and quality of services provided by RIAs to their clients. This includes the use of written contractual agreements to clearly define roles and responsibilities of outsourced service providers and conducting regular due diligence and on-going oversight of such service providers. RIAs are already required, as per these existing and well recognized and understood fiduciary duties, to take these actions and to document and report on the efforts to their clients and to independent fund boards. The overly prescriptive nature of the Proposal’s requirements will only introduce duplicate costs, incurred to comply with new technical regulatory requirements, without material change in the vendor selection process or the quality of service provider oversight conducted by RIAs. Imposing new and unnecessary compliance burdens on RIAs without any clear offsetting benefit to the clients of RIAs makes little sense.

To the extent that an RIA is not adequately overseeing its third party vendors in line with its existing fiduciary responsibilities, the Commission already has plenty of tools at its disposal to address such non-compliance, both through the Commission’s RIA examination program and its enforcement program. The Commission should utilize these existing methods to address observed deficiencies in third party vendor oversight rather than relying on additional regulatory mandates that will not appreciably enhance investor protection. We note, in this respect, that the absence of enforcement actions against RIAs by the Commission in relation to third party service provider oversight would seem to suggest that historically there have not been problems with RIAs exercising appropriate

diligence and oversight of outsourced service providers and that RIAs have in fact been operating broadly in line with their existing fiduciary duties with respect to third party vendor oversight. We believe that continued oversight by examination and enforcement, supported by tailored guidance to the extent required by the Commission, is a better approach than the adoption of this overly prescriptive and cost-creating Proposal. State Street therefore strongly urges the Commission to withdraw the Proposal.

EXCLUDE BANK CUSTODIANS FROM “COVERED FUNCTION”

To the extent that the Commission makes the decision to proceed with this rulemaking, State Street recommends that services provided by bank custodians to RIAs with respect to custody, fund administration and transfer agent services should be explicitly excluded from its scope. As drafted, the Proposal applies to the extent that an RIA retains a service provider to perform a ‘covered function’. What is not clear is whether custody and related administrative services fall within the definition of that term. While the Proposal provides a non-exhaustive list of potential covered functions,³ which leaves out the custody function, it also states that custodians that are “independently selected and retained” through a written agreement directly with the client are excluded from the Proposal’s scope, thus suggesting that when a RIA itself selects a custodian, the custody service provider would be in scope. We believe such a distinction should be eliminated, so that all custody services provided by a bank custodian, regardless of who chooses the custodian, are excluded from the Proposal. Additionally, although fund administration and transfer agent services are currently omitted from the definition of ‘covered functions’, the Commission asks whether such services should be subject to the Proposal.⁴ We do not believe that it is necessary to include such services within the Proposal’s scope. The Commission should therefore affirm that custody, fund administration and transfer agent services are excluded from the Proposal’s remit.

There are several reasons why services provided by bank custodians should be excluded from the scope of the Proposal’s intended due diligence and oversight requirements. First, a bank that is a qualified custodian under the Investment Advisers Act of 1940 are subject to stringent prudential mandates. This includes capital, liquidity, stress testing, and other financial resiliency requirements; cyber security and other operational resiliency obligations, recovery and resolution planning mandates; and anti-money laundering and financial crimes regulation. Furthermore, custody banks are subject to ongoing supervisory oversight and review by dedicated teams of on and off-site examiners. Such examinations are conducted on a routine basis and are designed to ensure that bank custodians operate in a safe and sound manner.

³ Potential covered functions listed by the Proposal include: Adviser/Subadviser; Client Services; Cybersecurity; Investment Guideline/Restriction Compliance; Investment Risk; Portfolio Management (excluding Adviser/Subadviser); Portfolio Accounting; Pricing; Reconciliation; Regulatory Compliance; Trading Desk; Trade Communication and Allocation; and Valuation.

⁴ Question 22 asks “Should services provided to a fund, such as fund administration, transfer agent, principal underwriter or custody services, be deemed to be “investment advisory services” or otherwise covered under the proposed rule and related recordkeeping requirements?”

Second, to comply with both regulations and supervisory expectations, custody banks have implemented and operate robust control frameworks which address, among other matters, the monitoring and management of capital and liquidity, counterparty due diligence practices, information systems and controls, third party risk management practices, business continuity plans and the maintenance of anti-money laundering and other financial crimes compliance infrastructure. In addition, banks, such as State Street, routinely undergo independent audits to ensure compliance with various prudential policies, procedures, and controls, and Sarbanes-Oxley reports are issued in relation to the effectiveness of the bank's control framework. State Street's business continuity plan and other similar requirements are also routinely tested for their effectiveness. As such, bank custodians offer their services to RIAs and other institutional investor clients in a manner that ensures a high degree of investor protection. Therefore, custody, fund administration, and transfer agent services provided by bank custodians should be excluded from the Proposal's scope in order to avoid overlapping and potentially conflicting regulatory requirements, with very limited incremental benefit.

CONCLUSION

Thank you once again for the opportunity to offer our comments on the Proposal. While we appreciate the Commission's desire to ensure that proper due diligence is conducted by RIAs on third party vendors, we believe the Proposal is unnecessary to properly manage these relationships, which are already subject to the RIA's fiduciary obligation to its clients. Furthermore, the Proposal's application to custody, fund administration and transfer agent services conducted by bank custodians is unnecessary due to the existing prudential and supervisory mandates to which banks are already subject and which provide a high level of investor protection to the clients of RIAs who utilize the services of bank custodians.

Please feel free to contact Joseph J. Barry at [REDACTED] should you wish to discuss State Street's submission in further detail.

Sincerely,



Joseph J. Barry
Global Head of Regulatory, Industry and Government Affairs
State Street Corporation



Sean O'Malley
General Counsel
State Street Global Advisors