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Submitted electronically to: rule-comments@sec.gov

May 2, 2019

Ms. Vanessa Countryman
Acting Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Investment Company Act Release No. 33329 (File No. S7-27-18); Fund of Funds Arrangements

Dear Ms. Countryman:

On behalf of our members, the Insured Retirement Institute ("IRI")[1] appreciates the opportunity to provide comments to the U.S. Securities and Exchange Commission (the "Commission") on the above-referenced rulemaking proposal, which is intended to streamline and enhance the regulatory framework for fund of funds arrangements (the "Proposal"). We support the Commission's efforts to create a more consistent and efficient rules-based regime for the formation and oversight of fund of funds arrangements, and we applaud the Commission for proposing a rulemaking that would provide a path for fund companies to access the potential benefits of fund of funds structures without first obtaining exemptive relief. Further, we believe that fund of funds arrangements are beneficial both to funds themselves as well as investors, and preserving the utility and benefits of these investment options is a critical consideration in this rulemaking process. We write solely to comment on one aspect of the Proposal relating to separate accounts funding variable insurance contracts.

Where a separate account funding variable insurance contracts invests in an "acquiring fund" for purposes of proposed Rule 12d1-4, the rule would require that the acquiring fund obtain a certification from the insurance company issuing the separate account that the insurance company has determined that the fees borne by the separate account, acquiring fund and acquired fund, in the aggregate, are consistent with the reasonableness standard set forth in Section 26(f)(2)(A) of the Investment Company Act of 1940 (the

[1] IRI is the leading association for the entire supply chain of insured retirement strategies, including life insurers, asset managers, and distributors such as broker-dealers, banks and marketing organizations. IRI members account for more than 95 percent of annuity assets in the U.S., include the top 10 distributors of annuities ranked by assets under management, and are represented by financial professionals serving millions of Americans. IRI champions retirement security for all through leadership in advocacy, awareness, research, and the advancement of digital solutions within a collaborative industry community.

"1940 Act").[2] The Proposal notes that the purpose of such a requirement is "to better protect investors from duplicative or excessive fees."[3]

We believe that the proposed certification requirement is unnecessary when viewed in the context of other existing statutory requirements and proposed conditions of Rule 12d1-4. We also believe that the requirement is contrary to the Commission's goal of creating a consistent regulatory regime for fund of fund arrangements, as this requirement would pertain only to fund of funds that are available as investment options under variable insurance contracts. In addition, we are concerned that this certification requirement would unduly introduce potentially significant logistical and other challenges and complications for these acquiring funds. We therefore ask that the Commission not include this requirement in any final rulemaking.

I. The Proposed Certification Requirement Ignores the Existing Statutory Requirements and Proposed Conditions of Rule 12d1-4

Under the existing statutory framework, Section 26(f)(2)(A) imposes a "reasonableness standard" on separate accounts funding variable insurance contracts. As part of determining whether a contract meets the "reasonableness standard," insurance companies evaluate the fees and charges deducted under the contract relative to the services rendered, the expenses expected to be incurred and the risks assumed by the insurance company.

The proposed certification is superfluous. At both the acquiring and acquired fund levels, the 1940 Act imposes meaningful checks and balances with respect to the establishment and ongoing imposition of advisory fees and certain other fund fees and expenses. Under Section 15(c) of the 1940 Act, the trustees of a fund have a "duty . . . to request and evaluate," and the fund's investment adviser has a duty "to furnish, such information as may reasonably be necessary to evaluate the terms" of an investment advisory contract, which involves information with respect to fund fees and expenses as deemed reasonably necessary by the trustees. After an initial term of up to two years, advisory agreements are subject to annual consideration and renewal. In each case, the agreements must be approved by vote of a majority of the independent trustees. In addition, Section 36(b) of the 1940 Act imposes a fiduciary duty upon an investment adviser with respect to the receipt of compensation for services or payments of a material nature paid by a fund or its shareholders to the adviser or its affiliates. These statutory provisions and Section 26(f)(2)(A) operate independently of one another and provide meaningful reviews of variable product and fund fees and expenses. Indeed, an insurance company should be entitled to rely on the oversight of fees and expenses by, and the fiduciary obligations of, funds of funds boards and advisers.

Among other conditions that would apply to acquiring funds relying on proposed Rule 12d1-4, an acquiring fund's adviser would be required to (i) evaluate the complexity of the structure and aggregate fees associated with the acquiring fund's investment in the acquired fund and (ii) find that it is in the best interest of the acquiring fund to invest in the acquired fund.[4] This condition would add another layer of

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[2] Under Section 26(f)(2)(A), a registered separate account funding variable insurance contracts, or a sponsoring insurance company, may only sell such a contract if "the fees and charges *deducted under the contract*, in the aggregate, are reasonable in relation to the services rendered, the expenses expected to be incurred, and the risks assumed by the insurance company" and "the insurance company so represents in the registration statement for the contract." (emphasis added).

[3] *See* Fund of Funds Arrangements, SEC Rel. No. IC-33329 (Dec. 19, 2018), 84 Fed. Reg. 1286 (Feb. 1, 2019), at 1305 (the "Proposing Release").

[4] *See* Proposed Rule 12d1-4(b)(3)(i). In addition, this evaluation and finding would be subject to board reporting requirements. We note that "acquired funds" under proposed Rule 12d1-4 are also subject to certain conditions with respect to investments in other funds.

fee and expense review to the existing statutory obligations of insurance companies, fund boards and fund advisers described above.

We believe that the proposed certification requirement would provide little added value to the robust, existing framework summarized above. At best, this requirement would be duplicative and redundant, largely echoing protections effectuated elsewhere.[5] In addition, it would impose an administrative burden on insurers and acquiring funds, which, in turn creates responsibilities for acquiring fund boards and acquiring fund management. This burden is not necessary and could prove to be a trap for the unwary.

II. <u>The Proposed Certification Requirement is Contrary to the Commission's Goal of a Uniform Regulatory Regime</u>

A stated goal of the Commission in the Proposal is to create a consistent rules-based regime for funds of funds and to level the playing field. As the proposed certification requirement would be uniquely imposed on acquiring funds within the variable insurance contract context, we believe that the requirement would be contrary to the Commission's stated goals. The mere fact that an acquiring fund is made available for investment through a variable insurance contract should not subject it to this different regulatory and compliance burden, which would only apply to its separate account investors (as opposed, for example, to qualified plans). Further, an acquiring fund made available through a variable insurance contract may be substantially similar, even nearly identical, to an acquiring fund available through non-insurance channels, yet the proposed certification requirement and its associated logistical and other challenges and complications would only apply to the former.[6] This outcome is incompatible with the notion of a level playing field.

Further, this provision would continue the troubling pattern of disparate regulatory treatment of insurance products and insurance-dedicated funds by the Commission and its staff. In this regard, consider that the Commission and its staff have never felt the need to adopt special rules to review whether different categories of investors in "retail" funds may have interests that compete with each other in some respect. However, for insurance products and their underlying funds, the Commission adopted rules and the staff implemented a regime called "mixed and shared funding" to set forth specific procedures for monitoring and dealing with potential conflicts among different categories of investors.[7] Consider also the Commission's impressive record of disclosure reform for mutual funds that led to the adoption in 2008 of a summary prospectus for funds, and compare that to the 10 additional years that it took for the Commission to propose a summary prospectus for variable contracts.[8]

III. <u>The Logistical and Other Challenges and Complications Outweigh Any Potential Benefits from the Proposed Certification Requirement</u>

We believe that the proposed certification requirement would unduly introduce potentially significant logistical and other challenges and complications for acquiring funds available as investment options under variable insurance contracts and for insurers. As noted above, the proposed certification requirement is based on a condition of existing exemptive relief for certain fund of funds arrangements.

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5 We recognize, though, that the proposed certification requirement is based on a condition of existing exemptive relief for certain fund of funds arrangements. However, we believe that the conditions of proposed Rule 12d1-4 render this requirement even more unnecessary than under the existing exemptive relief.

6 We note that a stated objective of the Proposal is to "create a more consistent and efficient regulatory framework for funds of funds than the existing regulatory framework" under which "substantially similar funds of funds are subject to different conditions." *See* Proposing Release at 1288, 1329.

7 *See* Rule 6e-2(b)(15) and Rule 6e-3T(b)(15), which provide exemptions from certain provisions of the 1940 Act only if a separate account invests "exclusively" in funds that offer their shares to certain limited offerees.

8 <u>Updated Disclosure Requirements and Summary Prospectus for Variable Annuity and Variable Life Insurance Contracts</u>, SEC Rel. No. IC-33286 (Oct. 30, 2018), 83 Fed. Reg. 61730 (Nov. 30, 2018).

However, the number of funds and fund companies that would be impacted by this condition (*i.e.*, funds that would be relying on proposed Rule 12d1-4) would likely be much greater than the number of funds and fund companies that operate in reliance on existing exemptive relief given, for example, the proposed rescission of Rule 12d1-2. Further, the proposed certification requirement could potentially place funds in a difficult business and legal and compliance position, particularly in the context of insurance companies that are not affiliated with the acquiring fund's adviser.

IV. Conclusion

We believe that the proposed certification requirement is unnecessary and inconsistent with Commission's stated goals in the Proposal. We urge the Commission to reconsider the proposed requirement and eliminate this condition from any final rulemaking.