Russell Investments

May 3, 2019

Vanessa Countryman
Acting Director, Office of the Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

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

Dear Ms. Countryman:

Russell Investment Management, LLC ("RIM")[1] appreciates the opportunity to comment, on behalf of Russell Investment Company ("RIC") and Russell Investment Funds ("RIF" and collectively with RIC, the "Registrants"), on the proposed rescission of Securities and Exchange Commission ("SEC" or the "Commission") Rule 12d1-2 and adoption of Rule 12d1-4 (the "Proposal") under the Investment Company Act of 1940, as amended (the "1940 Act"), which seeks to streamline and enhance the regulatory framework applicable to fund-of-funds arrangements.[2] We are writing to respectfully request that the SEC reconsider certain aspects of the Proposal in connection with any final rulemaking.

At the outset, we echo sentiments expressed in the comment letter (the "ICI Letter") submitted by the Investment Company Institute ("ICI") – an organization of which Russell Investments is a member – related to the proposed restriction on the ability of acquiring funds to redeem shares of acquired funds in certain circumstances.

1 RIM was established in 1982 and pioneered the "multi-style, multi-manager" investment method in mutual funds. As of December 31, 2018, RIM managed over $34.8 billion in 42 mutual fund portfolios.

2 *Fund of Funds Arrangements*, SEC Release No. IC-33329, 84 Fed. Reg. 1286 (Feb. 1, 2019), available at https://www.federalregister.gov/documents/2019/02/01/2018-27924/fund-of-funds-arrangements (the "Proposing Release").

I. *INTRODUCTION*

Each Registrant is organized as a Massachusetts business trust and is an open-end investment company registered under the 1940 Act. RIC and RIF currently offer 33 and 9 separate investment portfolios, respectively (each, a "Fund" and collectively, the "Funds"). The RIF Funds serve as investment vehicles for a variety of insurance products issued by one or more insurance companies. The RIC LifePoints Funds Target Portfolio Series (the "RIC Funds of Funds") comprise five series of RIC and the RIF LifePoints Funds Variable Target Portfolio Series (the "RIF Funds of Funds" and collectively with the RIC Funds of Funds, the "RI Funds of Funds") comprise four series of RIF.

Each RI Fund of Funds seeks to achieve its investment objective by investing principally in a combination of other RIC and/or RIF Funds (each, an "Underlying Fund" and collectively, the "Underlying Funds") to seek to provide investment diversification that an investor could otherwise achieve only by holding numerous individual investments.

To manage the RI Fund of Funds' overall exposures (such as asset class, currency, capitalization size, industry, sector, region, credit exposure, country risk, yield curve positioning or interest rates), RIM may cause an RI Fund of Funds to invest in derivatives, including futures, options, forwards, and swaps (the "Derivatives Positions"). Each RI Fund of Funds may also hold cash in connection with these investments and will usually, but not always, pursue a strategy of being fully invested by exposing its cash to the performance of segments of the global equity market by purchasing index futures contracts (known as "equitization" and collectively with the Derivatives Positions, the "Rule 12d1-2 Exposures"). The RI Funds of Funds invest any remaining cash in short-term investments, including the U.S. Cash Management Fund – an unregistered private fund advised by RIM.

Each RI Fund of Funds invests in the Underlying Funds in reliance on Section 12(d)(1)(G) of the 1940 Act and in the Rule 12d1-2 Exposures in reliance on flexibility afforded by the Commission under the current fund of funds regulatory regime. As a result, if the Proposal is adopted, the RI Funds of Funds would be required to either (i) divest the Rule 12d1-2 Exposures held in each RI Fund of Funds, thereby limiting RIM's ability to actively manage a Fund's overall exposures based on its desired preferred positioning, or (ii) restructure each RI Fund of Funds' target strategic asset allocation to provide sufficient flexibility to comply with the Rule 12d1-4 redemption limit.[3] However, as discussed in further detail in the following section, we do not believe that it will be possible to restructure each RI Fund of Funds to comply with the Rule 12d1-4 redemption limit and, by extension, continue to operate such Funds in a manner consistent with their current investment proposition. As a result, the Proposal would have negative consequences for the RI Funds of Funds and their respective shareholders.

II. FUND-OF-FUNDS ARRANGEMENTS, SUCH AS THE RI FUNDS OF FUNDS, SHOULD NOT BE SUBJECTED TO THE REQUIREMENTS OF PROPOSED RULE 12D1-4

RIM believes that the Proposal presents significant challenges to the continued viability of existing fund of funds arrangements. Under the Proposal, an acquiring fund holding shares of an acquired fund in excess of the Section 12(d)(1)(A) limits would generally be prohibited from redeeming or submitting for redemption (or tendering for repurchase) greater than three-percent of the acquired fund's total outstanding shares in any thirty-day period (the "3% Limit").[4] RIM expects that the RI Funds of Funds (as well as many other Same Group Fund-of-Funds Arrangements[5] which rely on the flexibility provided in Rule 12d1-2 under the 1940 Act to invest in unaffiliated acquired funds and non-fund assets) would be subject to the 3% Limit – the impact of which on such Funds' operations would be significant.[6] Therefore, to preserve the benefits of Same Group Fund-of-Funds

---

3 To the extent the Proposal is adopted, and the RI Fund of Funds invest a portion of its assets in one or more unaffiliated ETFs for cash management purposes in reliance on Rule 12d1-2 under the 1940 Act, the RI Funds of Funds would be faced with a similar choice.

4 As discussed in the Proposing Release, the 3% Limit would not apply to sales of an acquired fund's shares in a secondary market transaction. *See Proposing Release* at p. 192.

5 For purposes of this comment letter, the term "Same Group Fund of Funds Arrangements" refers to fund of funds structures in which a registered open-end investment company invests in one or more underlying registered open-end investment companies which are in the same "group of investment companies" as the acquiring fund.

6 For example, in the context of the RI Funds of Funds:

- For three of the five RIC Fund of Funds, a majority of each such Fund's investments in Underlying Funds represent more than three-percent of the Underlying Fund's outstanding shares.
- Although the RIC Conservative Strategy and Moderate Funds held on average only 1.75% and 2.36% of the outstanding shares (measures as a percentage of net assets) of their respective Underlying Funds, the three remaining RIC Funds of Funds hold on average approximately 10.6%, 12.7%, and 7.2% of

1301 2nd Avenue
18th Floor
Seattle, WA 98101
Tel 206-505-7877
Fax 206-505-3495
Toll-free 800-426-7969
russellinvestments.com
Seattle / New York / Toronto / London / Paris / Amsterdam / Dubai / Sydney / Melbourne / Auckland / Seoul / Tokyo / Shanghai / Beijing

Russell Investments

Arrangements cited by the Commission, RIM urges the Commission to consider the potential impacts of the Proposal on Same Group Fund-of-Funds Arrangements as well as the potential alternatives set forth below before adopting any final rulemaking.

1. *The Proposal Is Inconsistent with and Would Significantly Disrupt the Current Operation of Same Group Fund-of-Funds Arrangements*

At the outset, it is important to note that the Proposal would reverse the Commission's longstanding approach to regulating fund of funds arrangements. As discussed in greater detail in the ICI Letter, Congress enacted Section 12(d)(1)(G) of the 1940 Act to permit certain fund of funds arrangements. This statutory provision, which effectively codified the then-existing framework for fund of fund regulation imposed by the Commission through applicable exemptive relief, did not impose a redemption limit on the acquiring fund. Further, neither exemptive relief issued by the Commission following the adoption of Section 12(d)(1)(G) nor Rule 12d1-2 under the 1940 Act imposes such a restriction. Since the enactment of Section 12(d)(1)(G), many acquiring funds in existing Same Group Fund-of-Funds Arrangements have relied upon the flexibility provided by Section 12(d)(1)(G) and Rule 12d1-2 when structuring their underlying portfolio holdings. Thus, if the Proposal is adopted, it could have a number of significant negative consequences.

First, the Proposal could inhibit the formation of new investment products by fund sponsors. This would be particularly true for those products which are intended primarily to serve as underlying funds in a Same Group Fund-of-Funds Arrangement but would not be held by a sufficient number of acquiring funds or other investors to avoid triggering the 3% Limit with respect to such acquiring funds.

Second, the Proposal could hinder efficient portfolio management of Same Group Fund-of-Funds Arrangements, like the RI Funds of Funds, that rely on the flexibility provided in Rule 12d1-2

their respective Underlying Funds. Each RIF Fund of Funds also holds approximately 3% or more of the outstanding voting shares of at least one Underlying Fund.

- Similarly, the RIC Balanced Strategy, Growth Strategy, and Equity Growth Strategy Funds' largest single holding (measured as a percentage of Underlying Fund net assets) in an Underlying Fund is approximately 25%, 34%, and 24%, respectively. Under the Proposal, assuming no changes to the RI Funds of Funds' respective holdings as a result of market fluctuations or investment activity by other investors in the same Underlying Fund, it would take the relevant RIC Fund of Fund at least eight months to redeem its entire position in such Underlying Fund.

The foregoing information is as of March 29, 2019. The RI Funds of Funds' respective investments in the Underlying Funds may vary over time.

1301 2nd Avenue
18th Floor
Seattle, WA 98101
Tel 206-505-7877
Fax 206-505-3495
Toll-free 800-426-7969
russellinvestments.com
Seattle / New York / Toronto / London / Paris / Amsterdam / Dubai / Sydney / Melbourne / Auckland / Seoul / Tokyo / Shanghai / Beijing

under the 1940 Act to invest in unaffiliated funds and non-fund assets (such as the Rule 12d1-2 Exposures). Redemptions by an acquiring fund in such Same Group Fund-of-Funds Arrangements may, in the normal course, exceed the 3% Limit for reasons unrelated to efforts to influence control of the acquired fund, including portfolio holding rebalances to align the Same Group Fund-of-Fund's portfolio with its target strategic allocations, to implement target strategic asset allocation changes, to implement tactical asset allocation changes, or to implement allocations to new Underlying Funds. In such circumstances, restrictions on the ability to redeem shares of one or more underlying funds would limit the applicable portfolio manager's ability to implement his/her desired asset allocation and the acquiring fund's stated investment strategy. This could potentially negatively impact the RI Fund of Funds' performance, particularly if the portfolio manager is required to implement asset allocation changes at inopportune times.[7]

Furthermore, the 3% Limit may significantly impact each RI Fund of Funds' portfolio management as a result of requirements under the Funds' Rule 22e-4 liquidity risk management program (the "Program"). To the extent that fifteen percent or more of an RI Fund of Funds' portfolio holdings are deemed to be illiquid under the Program, the Program administrator would be required to determine and implement reasonable steps necessary to reduce the Fund's illiquid holdings below the fifteen-percent threshold. Under these circumstances, the Program administrator would have limited options available to reduce the RI Fund of Funds' illiquid investment holdings other than to sell shares of one or more of the Underlying Funds – a result which would further limit the applicable portfolio manager's ability to implement his/her desired asset allocation and the RI Fund of Fund's stated investment strategy. However, if the 3% Limit is in effect at the time when an RI Fund of Funds exceeds the 15% Limit, the Fund would be prohibited from taking this remedial action. As a corollary, during any period where fifteen percent or more of an RI Fund of Fund's portfolio holdings are deemed to be illiquid under the Program (which may occur with a degree of frequency), the Fund would be prohibited from acquiring additional shares of any Underlying Fund held in excess of the 3% Limit (whether as part of a portfolio rebalance, implementation of a new Underlying Fund allocation, or for any other reason). In these circumstances, the Proposal would severely curtail the investment proposition of such Funds as currently structured.

---

7 This assumes that an acquiring fund intended to hold three percent or more of the outstanding shares of an acquired fund. It is possible that due to market fluctuations or other factors outside the control of the portfolio manager to an acquiring fund, the acquiring fund may become a holder of greater than three percent of the outstanding shares of an acquired fund absent an intent to do so. Because the Proposal does not distinguish the mechanisms through which an acquiring fund becomes a greater than three-percent holder (*i.e.*, intentionally versus as a result of the redemption activity of other acquired fund shareholders), the same negative consequences discussed in this letter would apply to an acquiring fund which objectively has taken no action (nor had any intention of taking any action) triggering the policy concerns underlying the Proposal.

In light of these considerations, the Proposal would effectively require RIM to divest the RI Funds of Funds' Rule 12d1-2 Exposures. As a result, the RI Funds of Funds would no longer be able utilize the Rule 12d1-2 Exposures to equitize cash or to manage the RI Funds of Funds' overall exposures – a decision which could also have a negative impact on the RI Funds of Funds' performance. Thus, rather than improving oversight of fund of funds arrangements, the Proposal may reduce investment flexibility in favor of harmonizing the regime applicable to various fund of funds structures despite the Commission's own analysis indicating that the structures which would benefit most from the Proposal represent only a small percentage of the acquiring funds currently in existence.[8]

2. *Same Group Fund-of-Funds Arrangements Are Subject to Oversight Controls Which Mitigate the Policy Concerns Underlying the Proposal*

The Commission advanced a number of policy considerations underlying the Proposal which we believe are effectively mitigated in existing Same Group Fund-of-Funds Arrangements.

Threat of Large-Scale Redemptions

First, the 3% Limit is intended to:

- Address the concern that "an acquiring fund could threaten large-scale redemptions as a means of exercising undue influence over an acquired fund" and

- "[P]rovide a check against the influence that an acquiring fund can have on an acquired fund when it owns a significant percentage of the acquired fund."[9]

However, acquiring funds in Same Group Fund-of-Funds Arrangements (such as the RI Funds of Funds) are often managed to a pre-determined asset allocation among various underlying funds. In practice, this serves as an initial check on portfolio manager flexibility with respect to the extent to which an acquiring fund can invest in an underlying fund. Further, where an acquiring fund in a fund-of-funds arrangement invests substantially all of its assets in one or more acquired funds that share a common investment adviser, the SEC staff acknowledged that the investment adviser's fiduciary duty to both the acquiring and acquired funds mitigates the risk that a portfolio manager of the acquiring fund is acquiring a position in an acquired fund in excess of the Section 12(d)(1)(A)(i) limits to seek

8 *See* Table 1 on page 102 of the Proposing Release.

9 *Id*. at 47-48.

1301 2nd Avenue
18th Floor
Seattle, WA 98101
Tel 206-505-7877
Fax 206-505-3495
Toll-free 800-426-7969
russellinvestments.com
Seattle / New York / Toronto / London / Paris / Amsterdam / Dubai / Sydney / Melbourne / Auckland / Seoul / Tokyo / Shanghai / Beijing

to exercise control over the acquired fund, including through the threat of large-scale redemptions.[10] Third, in addition to the adviser's fiduciary duty, the fact that (i) the acquiring and acquired funds in a Same Group Fund-of-Funds Arrangement (such as the RI Funds of Funds) share a common board of directors/trustees and (ii) the nature of the Arrangement is disclosed via applicable registration statement disclosure,[11] serve as additional checks on an acquiring fund's ability to exercise control (including through the threat of large-scale redemptions) over another within the organizational umbrella.[12]

Confusion Regarding Applicable Conditions

The Proposing Release also indicates that the Proposal is intended to "create a more consistent and efficient regulatory framework for fund of funds arrangements" to:

- "[R]educe confusion and subject fund of funds arrangements to a tailored set of conditions that would enhance investor protection, while also providing funds with investment flexibility to meet their investment objectives in an efficient manner"; and
- "[E]liminate unnecessary and potentially confusing distinctions among permissible investments for different types of acquiring funds."[13]

---

10 *See id.* at 41 ("In circumstances where the acquiring fund and the acquired fund share the same adviser, the adviser would owe a fiduciary duty to both funds, serving to protect the best interests of both funds."). In fact, the Commission went a step further, acknowledging that even in circumstances where the advisers to the acquired and acquiring funds are control affiliates, there is a limited risk that the acquiring fund adviser would seek to control the acquired fund. *See id.* ("In addition, in cases where the arrangement involves funds that are advised by advisers that are control affiliates, we do not believe that the acquiring fund adviser generally would seek to benefit the acquiring fund at the expense of the acquired fund (nor do we believe that the acquiring fund would seek to influence the acquired fund through its ownership interest in the acquired fund")).

11 For example, such disclosure – which typically describes, among other things, the existence of such Arrangements and the individual underlying funds involved – has the practical effect of constraining the ability of a portfolio manager to an acquiring fund to seek to invest beyond disclosed target asset allocation levels and, by extension, to seek to obtain a significant position in an acquired fund (whether or not for the purpose of seeking to exercise control over such fund).

12 On the contrary, a fund sponsor (rather than an underlying fund portfolio manager) is more likely to modify the product characteristics of an acquired fund which serves primarily as an underlying investment vehicle in a Fund-of-Funds Arrangement to suit the investment needs of the acquiring fund.

13 *See id.* at p. 13, 17.

1301 2nd Avenue
18th Floor
Seattle, WA 98101
Tel 206-505-7877
Fax 206-505-3495
Toll-free 800-426-7969
russellinvestments.com
Seattle / New York / Toronto / London / Paris / Amsterdam / Dubai / Sydney / Melbourne / Auckland / Seoul / Tokyo / Shanghai / Beijing

However, many Same Group Fund-of-Funds Arrangements do not operate pursuant to Section 12(d)(1) exemptive orders. Instead, such Arrangements operate solely in reliance on Section 12(d)(1)(G) and, if necessary, Rules 12d1-1 and 12d1-2. In these circumstances, there is currently no risk of confusion of the conditions applicable to the relevant acquiring fund. In addition, it is unclear how the Proposal would further the Commission's goal of enhancing investor protection. Specifically, in light of the structural barriers to overreaching inherent in Same Group Fund-of-Funds Arrangements discussed above, RIM believes that the goal of investor protection appears to be served by the current regulatory regime.

Policy Considerations Underlying Section 12(d)(1) Generally

Section 12(d)(1) arose from a scenario where an individual, using a relatively small amount of money, acquired control of a fund and used the fund's assets to acquire control of the assets of another fund, which, in turn, could use its assets to control a third fund. As a result, a few individuals effectively could control millions of dollars in shareholder assets invested in various acquired funds. These "pyramiding" schemes were used to enrich the individuals at the expense of fund shareholders in a number of ways and masked fund shareholder's ability to understand either the scope of permissible investments by or person(s) controlling the funds into which it invested.[14] Taking into consideration the constraints on the actions of acquiring funds in Same Group Fund-of-Funds Arrangements set forth above, we also believe that the policy concerns underlying Section 12(d)(1) are effectively mitigated in the context of such Arrangements.

Taking into consideration the foregoing, RIM believes that the Proposal would have the effect of unnecessarily constraining legitimate Same Group Fund-of-Funds Arrangements, the very result which Section 12(d)(1)(G) of the 1940 Act and Rule 12d1-2 thereunder were adopted to seek to prevent. In the absence of specific evidence that existing Same Group Fund-of-Funds Arrangements raise Section 12(d)(1) policy concerns, we would urge the Commission to reconsider its Proposal.

III. POTENTIAL ALTERNATIVES TO THE PROPOSAL

In lieu of adopting Rule 12d1-4 as proposed, RIM suggests that the Commission, in connection with any final rulemaking, either:

- Eliminate the 3% Limit from any final rulemaking; or

14 See *Fund of Funds Investments*, Inv. Co. Rel. No. 26198.

- If Rule 12d1-4 is adopted as proposed, permit current Rule 12d1-2 under the 1940 Act and Rule 12d1-4 to operate side by side; or

- If any final rulemaking includes a 3% Limit, clarify that the 3% Limit would not apply to investments by an acquiring fund in an acquired fund which is in the same group of investment companies as the acquiring fund.

1301 2nd Avenue
18th Floor
Seattle, WA 98101

Tel 206-505-7877
Fax 206-505-3495
Toll-free 800-426-7969

russellinvestments.com
Seattle / New York / Toronto / London / Paris / Amsterdam / Dubai / Sydney / Melbourne / Auckland / Seoul / Tokyo / Shanghai / Beijing

IV. CONCLUSION

Based on the foregoing, RIM does not believe that the Proposal's expected impact on Same Group Fund-of-Funds Arrangements (including the RI Funds of Funds) is commensurate with the Proposal's stated policy objectives. Instead, we believe that any potential benefits derived from streamlining and enhancing the regulatory framework applicable to such Arrangements would be outweighed by the costs (both hard costs and costs associated with administrative distraction) incurred by fund sponsors. Therefore, absent a finding by the Commission or evidence from industry participants or investors suggesting that the current regulatory framework is no longer consistent with the policy objectives of Section 12(d)(1), we would encourage the Commission to not subject Same Group Fund-of-Funds Arrangements to heightened regulation and to implement one of the alternatives to the Proposal listed above.

Sincerely,

/s/ Peter Gunning

Peter Gunning
Chairman and President
Russell Investment Management, LLC

1301 2nd Avenue
18th Floor
Seattle, WA 98101

Tel 206-505-7877
Fax 206-505-3495
Toll-free 800-426-7969

russellinvestments.com
Seattle / New York / Toronto / London / Paris / Amsterdam / Dubai / Sydney / Melbourne / Auckland / Seoul / Tokyo / Shanghai / Beijing