

U.S. Securities and Exchange Commission
Asset Management Advisory Committee

Final Report and Recommendations for Small Advisers and Funds

November 3, 2021

I. Introduction

Based on input from membership of the SEC Asset Management Advisory Committee¹ (hereinafter the “AMAC”) regarding asset management industry priorities, the AMAC formed the Subcommittee on Small Advisers and Small Funds (hereinafter the “Subcommittee”). The asset management industry is largely comprised of small advisers and small funds, which provides important context as the Commission considers economic and competitive impacts of rulemakings and the overall regulatory landscape.² In addition, the AMAC and the Commission have each elevated and prioritized the goal of increasing and promoting diversity, equity, and inclusion in the asset management industry.³

¹ At the time of this recommendation, the SEC’s Asset Management Advisory Committee includes the following members: AMAC Chair, Edward Bernard, Senior Adviser, T. Rowe Price (former Vice Chair, TRP Corporate Board of Directors, former Chair of the Board of Directors of TRP Mutual Funds); John Bajkowski, President & CEO, American Association of Individual Investors; Jane Carten, President, Saturna Capital; Scot Draeger, President & General Counsel, R.M. Davis Inc.; Mike Durbin, President, Fidelity Institutional; Gilbert Garcia, Managing Director, Garcia Hamilton & Associates; Paul Greff, Chief Investment Officer, Ohio Public Employees Retirement System; Rich Hall, Deputy Chief Investment Officer, University of Texas/Texas A&M Investment Management Co.; Adeel Jivraj, Partner, Ernst & Young LLP; Renee LaRoche-Morris, Chief of Staff - COO/CAO, State Street Corporation; Susan McGee, Independent Director, Goldman Sachs BDC, Inc. (former President, U.S. Global Investors, Inc.); Jeffrey Ptak, Head of Global Manager Research, Morningstar Research Services; Erik Sirri, Professor of Finance, Babson College, Independent Director, Natixis Funds, Loomis Sayles Funds, and Natixis ETFs; Aye Soe, Managing Director and Global Head of Product Management, S&P Dow Jones Indices;; Rama Subramaniam, Head of Systemic Asset Management, GTS; John Suydam, Chief Legal Officer, Apollo Global Management; Russ Wermers, Chair of the Finance Department, Smith School of Business, University of Maryland; and Joe Savage, Vice President and Counsel in FINRA’s Office of Regulatory Analysis (non-voting member).

² See 2021 Investment Adviser Association Industry Snapshot: Evolution / Revolution Reimagined, 2nd Edition, July 2021, https://higherlogicdownload.s3.amazonaws.com/INVESTMENTADVISER/aa03843e-7981-46b2-aa49-c572f2ddb7e8/UploadedImages/publications/industry-snapshots/Investment_Adviser_Industry_Snapshot_2021.pdf. (hereinafter the “2021 IAA Report”). The 2021 IAA Report includes data on approximately 14,000 registered firms with over \$110 Trillion in assets for approximately 60 million clients. See also presentation of Karen Barr and Gail Bernstein made to the AMAC on September 27, 2021, <https://www.sec.gov/files/iaa-presentation-karen-barr-gail-bernstein-092721.pdf>. See also, testimony of Karen Barr, Gail Bernstein, Steve Yadegari, David Carson, Theresa Hamacher, and Russell Wermers at the AMAC meeting held September 27, 2021, <https://www.sec.gov/files/amac-092721-transcript.pdf>. See also presentation of Karen Barr and Gail Bernstein made to the AMAC on September 27, 2021, <https://www.sec.gov/files/iaa-presentation-karen-barr-gail-bernstein-092721.pdf>. See also, comments of SEC Commissioner Peirce and SEC Commissioner Lee at the AMAC meeting held on September 27, 2021, <https://www.sec.gov/files/amac-092721-transcript.pdf>.

³ See AMAC Recommendations to the U.S. Securities Exchange Commission on Diversity and Inclusion <https://www.sec.gov/spotlight/amac/amac-report-recommendations-diversity-inclusion-asset-managemenet->

The goals of assessing the impact of the regulatory framework on small businesses and promoting the growth of diversity, inclusion, and equity in the asset management industry, are not only aligned, but inextricably tied together.⁴ With these goals in mind, the Subcommittee’s purpose was the study of how the evolution of industry market structures and regulatory priorities have impacted the economic and operational challenges of small advisers and funds, and to identify areas where agency study, refined policy positions, guidance, and/or regulatory action(s) by the U.S. Securities and Exchange Commission (hereinafter the “Commission”) or the Commission Staff may further advance fair competition and growth of small and diverse businesses in the asset management industry, while also supporting core investor protections. As members of the Commission and the AMAC have highlighted, small advisers provide a bridge to prosperity as they engage on a daily basis with retail investors in communities across the country (including communities that have historically been on the sidelines of participation in the capital markets), i.e., these small advisers assist in capital formation, a goal of the SEC.⁵ Commissioners and AMAC members also commented on the importance of encouraging the growth of small firms and lowering barriers to entry and continued existence as consistent with the Commission’s mission.⁶ The AMAC remains dedicated to focusing recommendations on matters directly germane to the Commission’s mission, which it believes includes investor protection, market fairness, and encouragement of a market environment that is worthy of public trust.

II. Background on Small Asset Management Firms and Unique Regulatory Consideration

“Small” Advisory Firm and “Small” Fund Essentially Means the “Typical” SEC Registrant

It is important to define what we mean by “small firm” and “small fund” and to highlight that the vast majority of investment advisory firms registered with the Commission (including those firms that manage funds) are, indeed, “small firms.” The Investment Advisers Association (IAA) publishes an informative report each year that provides reliable data on the “shape” of the industry (compiled from an annual study of Form ADV filings). The *IAA 2021 Snapshot, Evolution Revolution Reimagined – “A Profile of the Investment Adviser Profession,”* (hereinafter, the “2021 IAA Report”)⁷ defines a “typical”

[industry.pdf](#). See also <https://www.sec.gov/files/amac-recommendations-di-subcommittee-07-07-21> (adopted in full by the AMAC on July 7, 2021). See also <https://www.sec.gov/files/amac-070721-transcript.pdf>.

⁴ See *id.*

⁵ See *Comments of Commissioners Peirce and Commissioner Lee* at the AMAC meeting held on September 27, 2021, <https://www.sec.gov/files/amac-070721-transcript.pdf>. See also AMAC discussions on September 27, 2021 and October 27, 2021, <https://www.sec.gov/files/amac-070721-transcript.pdf> and <https://www.sec.gov/files/amac-102721-transcript.pdf>.

⁶ See *id.*

⁷ See *2021 Investment Adviser Association Industry Snapshot: Evolution / Revolution Reimagined*, 2nd Edition, July 2021, <https://investmentadviser.org/wp-content/uploads/2021/10/investment-adviser-industry-snapshot-2021.pdf>. (hereinafter the “2021 IAA Report”). See also presentation of Karen Barr and Gail Bernstein made to the AMAC on September 27, 2021, <https://www.sec.gov/files/iaa-presentation-karen-barr-gail-bernstein-092721.pdf>. See also, testimony of Karen Barr, Gail Bernstein, Steve Yadegari, David Carson, Theresa Hamacher,

SEC-registered investment advisory firm (according to Form ADV-based data) as having the following shape:

- Most of its clients are individuals (on average two or fewer institutional clients)
- Average of \$355 Million in AUM
- Average of 9 employees (non-clerical)
- Average number of clients served is 3,149
- Average size of account of an individual investor around \$350,000

The investment adviser profession has always been dominated by small businesses.⁸ As highlighted in the 2021 IAA Report, of the approximately 14,000 SEC registered advisory firms, approximately 12,300 of those firms (almost 88%) reported employing 50 or fewer individuals in non-clerical positions and managing less than \$2 Billion in assets.⁹ Indeed, these businesses have humble revenues and tight budgets. More than half of the advisory firms registered with the Commission (both those who primarily manage funds and those primarily managing separately managed accounts) reported employing ten or fewer people.¹⁰ They are “small businesses” by any commonsense measure. The IAA 2021 Report also highlights that the majority of investment advisory firms are not located in New York, California or the largest of metropolitan areas; rather, firms are spread out throughout the country with most located in middle markets across the nation.¹¹ Despite the small size of the typical advisory firm, the investment advisory industry in aggregate is a powerful job creator, employing over 1,000,000 workers, largely in small businesses.¹²

Consistent with the data reviewed above, the AMAC considers the “typical” SEC registrant (under the Investment Advisers Act of 1940 and/or the Investment Company Act of 1940) to be a “small business” which likely has less than \$25 Million in annual revenue and significant budgetary constraints.

III. AMAC Observations on Economic and Operating Challenges of Small Advisers and Small Funds Relevant to Recommendations

As our panelists reinforced, small firms have challenges and opportunities that are often distinct from large firms.¹³ Furthermore, regional and local firms serving primarily individual investors (typically

and Russell Wermers at the AMAC meeting held September 27, 2021, <https://www.sec.gov/files/amac-092721-transcript.pdf>.

⁸ *Id.*

⁹ *Id.*

¹⁰ *Id.*

¹¹ *Id.*

¹² *Id.*

in their own communities) have business models that are entirely distinct from firms serving national or global institutional markets and typically involve activities that implicate a lower risk profile. For instance, the vast majority of advisory firms in this category do not manage derivatives or actively deploy strategies that involve holding a material allocation of securities with liquidity constraints.¹⁴ Nonetheless, despite deploying activities and strategies that typically involve less risk, regulatory compliance expenses, as a percentage of revenue, for these firms tends to be “outsized” as compared to the small number of large firms.¹⁵

¹³ See testimony of Karen Barr, Gail Bernstein, Steve Yadegari, David Carson, Theresa Hamacher, and Russell Wermers at the AMAC meeting held September 27, 2021, <https://www.sec.gov/files/amac-092721-transcript.pdf>. See also Presentation of Steve Yadegari, Chief Operating Officer and GC of Cramer, Rosenthal, & McGlynn, <https://www.sec.gov/files/cramer-rosenthal-mcglynn-presentation-092721.pdf>; Presentation of David Carson, SVP of Ultimus Fund Solutions and Trustee, Ultimus Managers Trust and Unified Series Trust, <https://www.sec.gov/files/ultimus-strengths-series-trusts-092721.pdf>; Presentation by Russell Wermers, Chair of the Finance Department, Smith School of Business, University of Maryland, *Technology & “Big Data”: Effects on Asset Manager Economies of Scale*, <https://www.sec.gov/files/technology-and-big-data-presentation-092721.pdf>.

¹⁴ See 2021 IAA Report, <https://investmentadviser.org/wp-content/upload/2021/10/investment-adviser-industry-snapshot-2021.pdf>. See also presentation of Karen Barr and Gail Bernstein made to the AMAC on September 27, 2021, <https://www.sec.gov/files/iaa-presentation-karen-barr-gail-bernstein-092721.pdf>. See also testimony of Karen Barr, Gail Bernstein, Steve Yadegari, David Carson, Theresa Hamacher, and Russell Wermers at the AMAC meeting held September 27, 2021, <https://www.sec.gov/files/amac-092721-transcript.pdf>. See also Presentation by Russell Wermers, Chair of the Finance Department, Smith School of Business, University of Maryland, *Technology & “Big Data”: Effects on Asset Manager Economies of Scale*, <https://www.sec.gov/files/technology-and-big-data-presentation-092721.pdf>; Presentation of Steve Yadegari, Chief Operating Officer and GC of Cramer, Rosenthal, & McGlynn, <https://www.sec.gov/files/cramer-rosenthal-mcglynn-presentation-092721.pdf>; and Presentation of David Carson, SVP of Ultimus Fund Solutions and Trustee, Ultimus Managers Trust and Unified Series Trust, <https://www.sec.gov/files/ultimus-strengths-series-trusts-092721.pdf>.

¹⁵ See testimony of Karen Barr, Gail Bernstein, Steve Yadegari, David Carson, Theresa Hamacher, and Russell Wermers at the AMAC meeting held September 27, 2021, <https://www.sec.gov/files/amac-092721-transcript.pdf>.

AMAC Observations¹⁶:

- Data Management and Internal Control Environments Leading to Outsourcing: The evolution of “big data” and data management practices are driving the need for the typical adviser and fund to outsource a growing level of operational, compliance, and even investment activities to third-party vendors.¹⁷
- Small Advisers and Small Funds Have Rapidly Decreasing Negotiating Leverage with the FinTech Industry: Consolidation among major FinTech providers is leaving the typical adviser/fund beholden to the price schedules and offerings of fewer providers, emboldened to charge more, while contractually shifting material risks and liabilities to the adviser/fund. FinTech pricing has increasingly shifted to annuitized model pricing and implicated a dramatic increase in the volume and amount of licensing fees needed to deploy operating, risk management, compliance and investment tools, together, creating new margin pressures. To a certain extent, the same is true regarding pricing mechanisms and tactics of the major data vendors.

¹⁶ The AMAC observations are based on a combination of member industry experiences, independent study by AMAC members, as well as the full scope of reports and testimony provided by panelists convened before the AMAC and related subcommittee meetings. See Presentation of the Subcommittee on Small Advisers and Small Funds to the AMAC on October 28, 2021, presented by Scot Draeger, President and General Counsel of R.M. Davis, Inc.; Renee LaRoche-Morris, Chief of Staff - COO/CAO, State Street Corporation, Susan McGee, Independent Director, Goldman Sachs BDC, Inc. (former President, U.S. Global Investors, Inc.), Jane Carten, President, Saturna Capital, and Russ Wermers, Chair of the Finance Department, Smith School of Business, University of Maryland, <https://www.sec.gov/files/amac-20211028-draft-recommendations-safc.pdf>. See also the dialogue among AMAC members at the AMAC meetings held on October 28, 2021 and September 27, 2021, <https://www.sec.gov/files/amac-102821-transcript.pdf>, <https://www.sec.gov/files/amac-092721-transcript.pdf>. See also 2021 IAA Report, <https://investmentadviser.org/wp-content/upload/2021/10/investment-adviser-industry-snapshot-2021.pdf>; Presentation of Karen Barr and Gail Bernstein made to the AMAC on September 27, 2021, <https://www.sec.gov/files/iaa-presentation-karen-barr-gail-bernstein-092721.pdf>. Testimony of Karen Barr, Gail Bernstein, Steve Yadegari, David Carson, Theresa Hamacher, and Russell Wermers at the AMAC meeting held September 27, 2021, <https://www.sec.gov/files/amac-092721-transcript.pdf>. Presentation by Russell Wermers, Chair of the Finance Department, Smith School of Business, University of Maryland, *Technology & “Big Data”: Effects on Asset Manager Economies of Scale*, <https://www.sec.gov/files/technology-and-big-data-presentation-092721.pdf>; Presentation of Steve Yadegari, Chief Operating Officer and GC of Cramer, Rosenthal, & McGlynn, <https://www.sec.gov/files/cramer-rosenthal-mcglynn-presentation-092721.pdf>; and Presentation of David Carson, SVP of Ultimus Fund Solutions and Trustee, Ultimus Managers Trust and Unified Series Trust, <https://www.sec.gov/files/ultimus-strengths-series-trusts-092721.pdf>.

¹⁷ For instance, a Morgan Stanley/Oliver Wyman report concludes that advances in data science and artificial intelligence may help streamline the investment and distribution processes, but only for a select few asset managers. The implication is that the majority of asset managers will increasingly outsource such efforts to lower costs or leverage more skilled intermediaries (or both). Further, this report indicates that “outsourced Chief Investment Officers” may dilute the value of in-house asset manager value-added. See “Wholesale Banks & Asset Managers: Winning Under Pressure,” Morgan Stanley/Oliver Wyman “Bluepaper,” available at <https://www.oliverwyman.com/our-expertise/insights/2018/mar/wholesale-banks-asset-management-analysis-2018.html>.

- Insurance Markets Are of Weakening Utility: While large firms can (and do) “self-insure,” the insurance industry is hardening for small firms. Insurance industry products (especially for cybersecurity/data security) provide little real protections for advisers/funds or their clients.
- Cybersecurity Costs Are Growing as a Percent of Revenue and Operating Costs for Small Firms: Costs and expenses associated with cybersecurity tools and protocols, as well as Business Continuity and Disaster Recovery technology tools are all becoming a much more significant expense as a percentage of revenue for small advisers/funds. While these expenses are also increasing in hard dollars for large firms, the impact is outsized for small firms, as both a percentage of operating expenses and a percentage of revenues.
- Outsourcing Shift Occurring Simultaneous with Loss of Leverage over Vendors: Outsourcing of “full economy” or “full operational chain” support is moving from a “choice” closer to a mandate in the context of business judgment of small adviser/fund boards and executive teams. For example, multiple series trust products (for funds) and outsourcing of full-chain middle- and back-office services for advisers is increasingly perceived as necessary to meet governance, operational, data management, and compliance demands. As a practical matter, due to leverage constraints, vendor due diligence is limited by the “curated” information offering of the vendor (summaries of SOC and SSAE reports).
- Standard Setting Defaults to “Institutional” Style of (and Tools for) Risk Management: Regulator perspective on “best practices” often mirrors/reinforces the approach taken by large institutional firms to risk management and compliance, setting expectations difficult to achieve (operationally or financially) for small advisers/funds.
- Balance Sheet Vise Is Tightening for Small Advisers and Funds: The growth of fixed costs¹⁸ for small advisers and small funds (including those representing barriers to entry) persists in an environment where fee compression is also ever-present. Both the revenue side and the expense side of the balance sheet are “closing in” on small firms. The cumulative costs of regulatory compliance efforts for small firms is a budget item that represents a growing fixed cost (in hard dollars) and is also growing as a percentage of both operating costs and revenue (growing year-over-year).
- Creativity Balanced with Budgetary Discipline Required to Meet Operating and Regulatory Demands: The approach small advisers/funds must take toward risk management and

¹⁸ Examples of regulatory compliance costs and efforts that represent fixed costs that are increasing year-over-year and also represent a growing expense as a percentage of revenue and/or total operating costs include, among other things: the cost of proxy voting and proxy voting advisory services; valuation tools; fund and SMA accounting and fee software; frequent fintech upgrades for performance reporting software and the cost of systems that maintain/validate data integrity in performance history; best execution reporting tools; back-up servers and cloud-based solutions for supporting disaster recovery and business continuity planning; custodial software tools for reconciling access-person personal trade review; cybersecurity measures such as multi-layer penetration testing and cybersecurity risk assessments; the cost of independent surprise custody examinations; general recordkeeping costs for 5-6 years’ worth of electronic data stored by data storage providers; developing and maintaining an independent derivatives risk management program; the costs of independent pricing service subscriptions (and the licensing fees they pass through/require); the costs of data management systems (and the licensing fees they pass through/require); and the cost of annual assistance in vendor due diligence and the DDQ regime.

compliance (as well as their approach to markets and counterparties) requires creativity and budgetary disciplines in order to account for a lack of leverage across all business needs, including access to “new issues” in the bond market, negotiation with FinTech vendors, licensing fee burdens, managing relationships with custodians, approaches taken to derivatives risk management, access to research, and deployment of cybersecurity tools (just to name a few).

- Economic Analysis Remains a Critical Part of the SEC Rulemaking Process: The economic analysis done in the context of rulemaking initiatives and proposals that the Administrative Procedure Act and Regulatory Flexibility Act require is critical work that remains truly relevant to the Commission’s informed consideration of the impact of rules and regulations (individually or in aggregate) on the everyday lives and work of most investment advisory firms. Given the reality that nearly all firms with material gender and racial diversity among the owner group are small firms, the implications of the economic impact of regulation on small businesses is important if our industry is serious about facilitating growth of diversity in the asset management industry.
- Existing definitions of “Small Business,” “Small Organization,” and “Small Entity” utilized by the SEC in Conducting Economic Analysis in Connection with Rulemaking are Severely Outdated.
 - For example, Rule 0-7 promulgated under the Investment Advisers Act of 1940 (the “Advisers Act”) defines “small entities” under the Advisers Act for purposes of the Regulatory Flexibility Act, to be those with \$25 million or less in Assets Under Management (AUM). Given that the basic threshold for SEC registration is currently \$100 million in AUM, very few SEC-registered advisers are deemed to be “small” for purposes of analysis under the Regulatory Flexibility Act. Similar definitional insufficiencies exist in other relevant rules describing “small business” and “small organization” as they pertain to registered investment advisers. Current definitions originally intended to capture small businesses are entirely insufficient and do not help the Commission to fulfill important regulatory policy goals of assessing economic impact on small businesses in the investment management industry.
- Agency “Connection” with Cumulative Impact of Regulations on Small Business is Missing: The Commission’s Division of Economic & Risk Analysis, historically, has engaged primarily in a rule-by-rule analysis of economic impacts (including assessment of the impact on small businesses in our industry). Given the breadth, scope, and depth of the regulatory requirements on all registrants and considering the growing aggregate or cumulative impact of compliance costs on the balance sheet health of small advisers/funds, economic analysis done in a vacuum has limited utility. While economic analysis on a rule-by-rule basis is necessary, it is insufficient to provide the Commission (and public commenters) the picture necessary to be fully informed in considering and commenting on rulemaking initiatives.
- Specific Areas Where Regulatory Action may be Lagging or Disconnected from Market Realities¹⁹: *The regulatory regime seems either to be lagging market needs, and/or disconnected*

¹⁹

See id.

from market realities in the following specific areas where those realities may also be disproportionately impacting small firms (e.g., firms with “typical,” but limited, resources):

- Bond Market Access: There is growing “inaccessibility” (for both small advisers/funds and retail investors) to “new issues” in the Bond market, that has been exacerbated by other market developments, such as the expansion of the private debt markets (e.g., 144A offerings not being available to individual investors and the typical registered advisory firm/small fund). Because bond issuers have economic incentives to collaborate with institutional investors (who also have heightened access to the private markets), as the public market for “new issues” retracts, there is not a level playing field for individual investors or the typical investment adviser or fund to gain access to quality “new issues” in the bond market. It does not appear that sufficient action is being taken to facilitate and promote continued growth of the public market for quality new issues in the bond market.²⁰
- Full Conversion to E-Delivery / E-Signatures: E-delivery for notices, disclosures, approvals and signatures are still not permitted as the “default.” While universally accepted by regulators of other industries (including banking regulators), electronic delivery and electronic signatures still are not permitted as the “default” for advisers and funds.
- Data Security Legal Regime: The legal regime for data protection, data security, and customer notice/remediation protocols remains balkanized. There remains a disparate array of data security regulations existing in 50 states, as well as those promulgated by a variety of federal regulators (as well as foreign regimes). The disparity in approaches seems to be growing, as each jurisdiction or regulator works to adjust regulations to a rapidly changing ecosystem of cyber threats and notice/remediation approaches relative to adverse impacts of cyber events.

²⁰ Even in the public markets, the largest firms, largest funds, and institutional investors (pension funds, large endowments, etc.) have established “channels” needed for obtaining “new issues” in the investment grade corporate and municipal bond market ahead of small firms and retail investors. Small firms cannot simply rely on the bond fund market to fulfill their client needs. Many small firms believe it is in their clients’ best interest to build a ladder of individual bonds, rather than seek exposure to the fixed income markets through bond funds. The intent is often to hold bonds to maturity as a method of supporting client income needs in retirement, not to actively “trade” bonds. Smaller advisers managing separate accounts for individuals or small fund advisers generally do not have multi-layered business relationships with the lead underwriters, enabling easy access to high quality corporate and municipal bond new issues. As a result, even in the public markets, small advisers can find it hard to obtain access to the highest quality issuances at the issue price because the institutional market participants have positioned themselves to “take down” most of the offering. This leaves individual investors in a position of having to overpay for the limited inventory available in the secondary market. Once you add to this the reality that the bond offerings are increasingly being issued through private (rather than public) markets, the playing field becomes increasingly unfair.

- Cybersecurity: There is a widening gap between regulatory expectations on deployment of cybersecurity measures relative to the resources available for small firms/funds.
- Liquidity Rule and Derivatives Risk Management: Governance confusion persists regarding the appropriate delineation of responsibilities between/among the fund board, the fund’s adviser, and the derivatives risk manager, as well as how these responsibilities relate to similar responsibilities under the liquidity risk management program.
- Proxy Voting: There is continuing “disconnect” on use of proxy voting advisory services by advisers and funds as a method of fiduciary fulfillment. Recent Commission guidance has materially increased the cost of deploying resources necessary by the typical adviser/fund, while decreasing the ability of advisers/funds to rely on those resources. Furthermore, the focus and emphasis given to the battle between large public issuers and activist/institutional investors led the Commission in a direction that left small investment advisers and funds (and their clients) as casualties.
- CUSIP and Benchmark Index Licensing Fees²¹: License needs and fees linked to agency regulations are a growing problem. The CUSIP license fee regime has far “overreached” in the imposition of fees on advisers and funds, especially when advisers/funds only use the CUSIP numbers for internal recordkeeping and client reporting. Similar issues exist

²¹ CUSIPs are nine-digit alphanumeric codes which the US numbering agency assigns to identify US equity and fixed-income securities. CUSIP numbering is referenced in SEC rules and is critical to issuing, trading, and clearing transactions in US securities, as well as regulatory reporting. CUSIP Global Services also assigns 12-digit alphanumeric international securities identification codes to the same US securities. The acronym CUSIP derives from the Committee on Uniform Security Identification Procedures, a committee of the American Bankers Association (“ABA”). S&P Capital IQ operates CUSIP Global Services under a contract with the ABA, which owns the intellectual property rights to CUSIPs. Issuers of securities pay CUSIP Global Services to assign them CUSIPs for their securities, which is logical to the AMAC and the market at large. CUSIP Global Services also charges the same issuers to use the CUSIPs in final official statements, tax forms filed with the Internal Revenue Service and any letters of representation needed to register securities in book-entry form with Depository Trust Company (“DTC”), the US national securities depository. This is also understandable to the AMAC. What offends the advisory/fund industry (especially the small adviser/fund community), however, is that all firms which trade and process transactions in securities identified by CUSIPs must pay separate licensing fees to store the CUSIPs internally in securities master files and other databases as well as use them for client-facing, recordkeeping and regulatory needs, such as trade confirmations, account statements and regulatory reporting. The licensing fees charged by CUSIP Global Services to small advisory firms depends upon the number of CUSIPs stored, the number of business lines using the CUSIPs, and the regions in which the CUSIPs are used. CUSIP Global Services appears to have a monopoly on the securities identification system and the advisory/fund industry (particularly small advisers/funds) currently has no reasonable alternatives. Furthermore, CUSIP Global Services has used its leverage with the entire market of FinTech firms to have the FinTech firms contractually require advisory firms and funds to agree to pay such licensing fees as a condition of contracting with the FinTech firms (with whom small advisers/funds have no leverage to negotiate). Even if an adviser/fund does not need access to the CUSIP itself, in many cases (such as where research is shared through typical mediums, such as FactSet) the CUSIPs cannot be stripped from the research and license fees are demanded by FinTech provider (on behalf of CUSIP). These practices, in addition to being fundamentally unfair, would seem to violate legitimate public policy considerations.

in the licensing regime for securities index providers. European regulators have been much more proactive with policy positions and regulatory actions that seek to curtail the overreach, including actions limiting the manner and amount of fees charged for securities identifiers used by market participants for internal maintenance and reconciliation of master securities files.

There is, of course, a universal desire (by both the small firm advisory and fund community and the Commission) to navigate these challenges in a manner that promotes investor protection and also provides a balanced regulatory approach that allows for growth of small businesses. That said, finding that balance requires the genuine desire to appreciate the challenges of the community of small advisers and funds.

IV. AMAC Recommendations to the SEC on Matters Impacting Small Business Registrants in the Asset Management Industry (Small Advisers and Small Funds)

1. **Modernize the definitions of “Small Business,” “Small Organization,” and “Small Entity” utilized by the SEC in conducting economic analysis in connection with rulemaking:** The AMAC recommends that the Commission modernize the definition of “small entities” for Regulatory Flexibility Act considerations. The AMAC also recommends that the Commission modernize other definitions (such as “small organization” and “small business”) relevant to the universe of firms captured in assessing economic analysis and impact on investment advisers and funds operating as small businesses in the context of SEC rulemaking. The AMAC recommends that the Commission acknowledge that AUM is an ineffective measure, particularly when applied exclusively, in identifying “small businesses.” Consideration of human and financial resources available to operate a business has much greater utility. As applied to advisers, for example, we believe the Commission should consider defining “small business,” “small entity,” and “small organization” to mean any registrant with fewer than 50 employees or annual revenue of less than \$25M.²² As applied to investment companies (funds), we believe the Commission should consider defining “small business,” “small entity,” and “small organization” to capture any fund with a principal adviser to a fund that has fewer than 50 employees or annual revenue less than \$25M.²³
2. **Modernize Economic Analysis and Reporting:** The AMAC recommends that the Commission, through the Division of Economic & Risk Analysis, conduct periodic assessments and make

²² We appreciate that Form ADV does not currently collect information on revenue of registered investment advisers; however, we believe it would be simple enough to incorporate a question that asks firm’s to simply identify whether the firm had less than \$25 Million in revenue for the annual reporting period.

²³ Once again, we realize that Investment Company Act filings do not currently collect information on revenue of the principal investment advisers to investment companies; however, we believe it would be simple enough to incorporate a question that simply identifies whether the principal adviser to the fund had less than \$25 Million in revenue for the annual reporting period (as well as soliciting whether the principal adviser to the fund has fewer than 50 employees).

periodic reporting on the cumulative impacts of regulation on small advisers and funds (conducted every 5 years). The AMAC recommends that the Commission engage in public reporting on the cumulative impacts of regulation on small advisers and small funds.

3. Bond Market Study: The AMAC recommends that the Commission convene a Roundtable to study the drivers of the growing “inaccessibility” (for both small advisers/funds and retail investors) to “new issues” in the bond market, that has been exacerbated by other market developments, such as the expansion of the private debt markets (*e.g.*, 144A offerings), which are less accessible to individual investors and the typical registered advisory firm/small fund). The goal should be to facilitate a level playing field for individual investors (and the typical investment advisory firm/fund) to gain greater access to quality “new issues” in the bond market and to determine what action can be taken to promote continued growth of the public market for quality “new issues” in the bond market.
4. E-delivery and E-Signatures: The AMAC recommends that the Commission move swiftly to make it legally acceptable for investment advisers and funds to utilize an electronic delivery regime for delivery of all notices, disclosures, and information as the default method of delivery of required information, with the right of any investor to opt out and continue to receive paper (*e.g.*, no affirmative consent required for e-delivery). We also recommend that the Commission move swiftly to make it legally acceptable for investment advisers and funds to utilize electronic signatures for all client contracts, consents, and approvals of any nature; once again, as the default practice (with an opt-out opportunity, but no affirmative consent required for the default).
5. Regulatory Coordination on Data Security and Privacy: We recommend that the Commission’s Office of Legislative Affairs take an advocacy role in encouraging Congress to establish a data security and privacy law regime applicable to the financial services sector, centralized at the federal level.
6. Calibrate Guidance on Cybersecurity, Business Continuity, and Disaster Recovery: We recommend that the Staff or Commission consider issuing guidance on “best practices” in these three important areas that is tailored separately to large enterprises and small businesses.
7. Proxy Voting by Small Advisers and Small Funds: The AMAC recommends that the Commission and Staff consider their work on the use/reliance of/on proxy voting advisory firms as unfinished. We recommend that Commission and Staff fully consider the extent to which reliance on the issuer diligence and recommendations performed/made by proxy voting advisory firms enhances (rather than detracts from) the ability of small advisers and funds to fulfill their fiduciary duty in the context of proxy voting.
8. Liquidity Rule and Derivatives Risk Management Program: There continues to be confusion on the balance of governance and oversight by the fund board (relative to the role of the investment adviser to the fund and the derivatives risk manager) in the context of the Derivatives Risk Management Program, as well as how these responsibilities relate to similar

responsibilities under the liquidity risk management program. While, under the rule, the fund's investment adviser is not eligible to serve as the derivative risk manager, fund boards report interest in more guidance in relation to the role of the fund's investment adviser relative to the derivatives risk manager and the delineation of duties between the fund board, fund adviser, and derivatives risk manager. The AMAC recommends that the Commission or Staff issue further guidance in this area that merges an "activity-based" approach with a "risk based" and "resource-based" approach.

9. CUSIP and Index License Fee Regime: The AMAC recommends that the Commission study whether to remove specific reference to "CUSIP" relative to securities identifiers in its rules and regulations.²⁴ We also recommend that the Commission study whether it has legal jurisdiction to regulate CUSIP and securities index licensing fee practices as they pertain specifically to fee imposition on investment advisers and funds. If statutory authority exists, we recommend the Commission take regulatory action to limit the licensing fees charged to the issuers of the securities identified by the CUSIP number and, with respect to securities indices, limit licensing fees to circumstances where an adviser or fund is using reference to the index in an advertisement or in the name of a fund or strategy (and not in connection with regulatory and client reporting, or internal purposes).²⁵ Even if the Commission determines that there are statutory or jurisdictional limitations on its ability to act on this, the Commission should take a formal public policy position and coordinate with the FTC in exploring the impact of current monopolies that may exist, as the European regulators have done. This is an issue of material import to the typical registrant.

V. Conclusion

AMAC's recommendations focus exclusively on matters directly germane to the Commission's mission, which includes investor protection, market fairness, and encouragement of a market environment that is worthy of public trust. We approached this work with dedication to serving the investing public, the industry, the Commission, and advancement of the integrity of U.S. capital markets.

As provided at the outset, the focus of the AMAC in this area has been the study of how the evolution of industry market structures and regulatory priorities have impacted the economic and operational challenges of small advisers and funds and to identify areas where agency study, refined policy positions, guidance, and/or regulatory action(s) by the Commission or the Commission Staff may further advance fair competition and growth of small and diverse businesses in the asset management industry, while also supporting core investor protections. Small advisers provide a bridge to prosperity as they engage on a daily basis with retail investors in communities across the country (including communities that have historically been on the sidelines of participation in the capital markets). The

²⁴ The Commission could consider use of other standard identifiers created by the Commission (preferably) or the exchanges; although currently, no alternative and widely accepted identification system exists. We do note that making a change in securities identification systems would impose costs on firms to modify their systems, so study of the issue first would be important.

AMAC believes the importance of encouraging the growth of small firms and lowering barriers to entry and continued existence is consistent with the Commission's mission. The AMAC believes the recommendations contained in this report, if acted upon, would further these important goals, without weakening investor protection.