April 7, 2014

By email

Secretariat of the Financial Stability Board
c/o Bank for International Settlements
CH-4002
Basel, Switzerland

Re: Financial Stability Board ("FSB") and International Organization of Securities Commissions ("IOSCO") Consultative Document, Assessment Methodologies for Identifying Non-Bank Non-Insurer Global Systemically Important Financial Institutions, 8 January 2014

Dear Sir or Madam:

The Association of Institutional INVESTORS (the "Association") appreciates the opportunity to provide the FSB and IOSCO with its comments regarding the Consultative Document (hereinafter, the "Document") proposing assessment methodologies for identifying non-bank non-insurer ("NBNI") global systemically important financial institutions ("NBNI G-SIFIs"). We agree with the focus on systemic risk but are concerned that the potential designations of individual investment funds as NBNI G-SIFIs may not address any systemic risks that may arise in regard to investment funds. The Association, as outlined in this letter, believes that any consideration of investment funds should be based on an activities-based approach that takes into account principles of comity, market-wide activities and existing regulatory regimes under which investment funds operate in particular jurisdictions.

The Association consists of some of the oldest, largest, and most trusted institutional investment advisers. While our firms are all registered with the U.S. Securities and Exchange Commission ("SEC"), we operate globally and serve clients around the world. Our clients are primarily institutional investment entities that serve the interests of individual investors through public and private pension plans, foundations, and registered investment companies. Collectively, our member firms provide advisory services to more than 80,000 pension plans, mutual funds, and similar investment entities on behalf of more than 100 million workers and retirees. Our clients rely on us to prudently manage participants' retirements, savings, and investments. This reliance is built, in part, upon the fiduciary duty owed to these organizations and individuals. As such, the Association is uniquely positioned to provide insight regarding the institutional investment advisory and collective investment vehicle industry and the Document's analysis of the industry's potential vulnerabilities and risks.

## 1. The G20 Leaders' Mandate to the FSB and IOSCO Did Not Direct the Designation of Any Investment Fund as a NBNI G-SIFI

In December 2011, the G20 Leaders' Declaration ("2011 Declaration") stated that "[w]e are determined to make sure that no financial firm is 'too big to fail' and that taxpayers should not bear the costs of resolution."[1] Toward that end, the 2011 Declaration mandated that the FSB in consultation with IOSCO prepare methodologies to identify systemically important non-bank financial entities.[2] In September 2013, the G20 Leaders' Declaration ("2013 Declaration") similarly requested that the FSB and IOSCO prepare public consultation methodologies for identifying global systemically important non-bank non-insurance financial institutions.[3]

Both the 2011 and 2013 Declarations call for a careful, analytically rigorous review by the FSB and IOSCO of non-bank non-insurance financial institutions to determine whether certain of such institutions could constitute global systemically important financial entities. In order to meet the Declarations' objectives the analysis should be transparent, rigorous, factually based and analytically sound.

The Association supports the overall goal of protecting the financial system against systemic risk. We are, however, concerned with the potential for unintended consequences and adverse impact of misplaced regulation. In this regard, the Association is firmly opposed to the designation of one or more investment funds as NBNI G-SIFIs. We believe that if a transparent and open comment process is followed, the FSB and IOSCO will conclude that investment funds are not a proper category for a sector-specific methodology ("Investment Fund Methodology").

Therefore, we respectfully request that the FSB and IOSCO reconsider whether investment funds should be one of the types of NBNI financial entities that should be evaluated for NBNI G-SIFI designation. We respectfully request that the FSB and IOSCO withdraw the Investment Fund Methodology and give further consideration to the issues, facts and analyses set forth in this letter.

## 2. The FSB and IOSCO Should Undertake Further Review and Consideration

The Association is concerned that the G20 mandate to determine whether any NBNI entities should be designated as NBNI G-SIFIs has been improperly interpreted as a mandate to

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1 Cannes Summit Final Declaration, paragraph 28.

2 *Id*. at paragraph 29.

3 Saint Petersburg Summit G20 Leaders' Declaration, paragraph 70.

designate one or more investment funds as NBNI G-SIFIs. The Leaders' Declarations contained no expression that the Leaders had considered or reached a conclusion whether, investment funds should be designated as NBNI G-SIFIs.

Nevertheless, the Document contains what appears to be a pre-ordained conclusion that investments funds are entities that are appropriately suited for designation as NBNI G-SIFIs without having provided any compelling evidence for such conclusion or seeking public input as to NBNI sectors that should be appropriately identified. The Document states that the three NBNI financial entity categories (investment funds, finance companies and securities dealers) that were identified were chosen due to their "relatively large size in the non-bank financial space" and "given historical examples of financial distress or failures in these three sectors that had an impact on the global financial system."[4] However, the Document does not explain how size alone correlates to the risk of significant disruption to the global financial system and economic activity across jurisdictions, and the Document provides no historical examples of distress or failure, broken-down by financial entity type or otherwise, that would be considered in concluding which financial entity types are appropriately suited for designation as NBNI G-SIFIs. Consequently, the apparent conclusion that investment funds are an appropriate sector for designation as NBNI G-SIFIs should be reconsidered in light of the comments received from, and issues raised by, the investors and companies that stand to be negatively affected by the proposed Investment Fund Methodology.

Furthermore, the Document does not provide reasonable support for an Investment Fund Methodology with an initial filter of a materiality threshold premised solely on the size of an investment fund. Most importantly, the Document does not take into account principles of comity, market-wide activities and the regulatory regimes under which investment funds operate in particular jurisdictions.

In this regard, we note that under the size criteria contained in the Investment Fund Methodology it appears that only U.S. domiciled investment funds would be considered for an NBNI G-SIFI designation. In this context, it is especially notable that the Document is devoid of any discussion of the comprehensive regulatory scheme imposed on registered investment companies by the U.S. Investment Company Act of 1940 ("ICA") ("U.S. registered funds").[5] The Association notes that these U.S. registered funds have been successfully administered by the SEC for over seventy years.[6]

4 Document at 7.

5 Our comments regarding "U.S. registered funds" in this letter apply to open-end, floating net asset value ("NAV") funds, not money market funds. The U.S. Financial Stability Oversight Council has recommended to the SEC that it implement reforms regarding the regulation of money market funds. In June 2013, the SEC responded by issuing for public comment proposed rules designed to reform money market fund regulation.

6 In this regard, we note that banks in the United States operate collective or common trust funds for the investment of customer funds. Such funds are not subject to registration as investment companies with the SEC under the ICA. Rather, they are subject to regulation under similar principles by the U.S. Office of the Comptroller of the Currency, the U.S. Federal Reserve Board or U.S. state banking authorities. Thus, comments in this letter regarding U.S. registered funds are generally applicable to such bank operated funds.

Given these fundamental deficiencies, we believe that it is critical that the FSB and IOSCO conduct further study as to whether investment funds do, in fact, merit consideration as NBNI G-SIFIs. In this regard, we recommend that the FSB and IOSCO take an alternative approach of evaluating the sufficiency of national regulation of investment funds in individual jurisdictions and considering whether to recommend particular enhancements of the investment fund regulation structure in individual jurisdictions to address the potential for systemic risk in the investment fund industry associated with market-wide practices. Finally, we suggest that a revised study should provide a full discussion of the information that the FSB and IOSCO have considered and an explanation of their analysis so that public input and comment can be appropriately focused, informative and beneficial to the FSB and IOSCO and their important work.

### A. The FSB and IOSCO should undertake further study to evaluate whether an approach to identifying NBNI G-SIFI investment funds based on their size, complexity and interconnectedness is supportable

The Association understands that the overarching objective of the Document is to identify NBNI financial entities whose "distress or disorderly failure, because of their size, complexity and systemic interconnectedness, would cause significant disruption to the global financial system and economic activity across jurisdictions."[7]

The Document appears to base the decision to identify investment funds as one of only three categories of NBNI entities that the FSB and IOSCO initially plan to evaluate for potential NBNI G-SIFI designations on the ground that investment funds trigger two systemic risk transmission channels. First, that investment funds may act as G-SIFIs based on their potential to generate loss exposures to counterparties and second, that investment funds may adversely impact particular asset markets as a result of the forced liquidation of positions in response to runs.

The Document provides only a cursory discussion of these two purported transmission channels and contains no empirical support for basing such a significant decision on either of the two identified transmission channels. In fact, the Document notes that, even during the 2008 financial crisis, mutual fund liquidations did ***not*** cause a systemic market impact. As discussed in Section 3 below, we believe that additional analysis of the investment fund industry, which gives proper attention to the suggestions and to the issues, facts and analyses set forth in this letter, would lead to the conclusion that U.S. registered funds do not pose the type of threat that would support treating such funds as a category of entities to be considered for NBNI G-SIFI designations.

To the extent that the FSB and IOSCO determine to proceed with an approach that would designate certain investment funds, we believe that it is essential that they carefully reevaluate whether the proposed Investment Fund Methodology is an appropriate standard on which to base designation as an NBNI G-SIFI.

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7 Document at 2.

In that regard, the Document's proposed initial filter ***size*** of $100 billion in net AUM for investment funds is not an appropriate indicator for evaluating systemic risk. The Document does not provide any data to demonstrate that an investment fund's size has any relevancy on whether its liquidation would be disorderly and costly to taxpayers. Frankly, the Association is concerned because a designation based on this threshold filter would capture ***only*** U.S. registered funds. These are the funds that are currently subject to an extensive regulatory regime that mitigates the risk of failure and manages a failure so that it would not be disorderly or costly to taxpayers.

The Association believes that the FSB and IOSCO should focus on the more appropriate and significant indicator of leverage, in particular leverage within a certain market segment of sufficient scale. It is leverage that magnifies the potential impact of an entity's failure, not the size of an investment fund. If the FSB and IOSCO were to maintain that certain investment funds should be designated as NBNI G-SIFIs, the initial materiality threshold should focus on the degree of leverage that such an investment fund employs rather than its size. However, data on leverage from a single investment fund is not sufficient to evaluate systemic risk. The FSB and IOSCO should consider how to obtain aggregated data on exposures and leverage across the industry to appropriately assess potential risk due to leverage in the markets.

**B. Any further study should focus on recommendations for national sectoral enhancements.**

The Association suggests that the FSB and IOSCO should conduct additional study which focuses on recommendations for national sectoral enhancements of the regulation of investment funds, taking into account existing regulations in an investment fund's home country and the types of activities in which a fund is engaging. As noted in the Document, NBNI financial entities often have different legal forms, business models and profiles which therefore make it difficult for the FSB and IOSCO to apply consistent standards for identifying G-SIFIs.[8]

The Document further acknowledges that a sectoral activities-based approach for assessing investment funds could be a possible alternative to the entity-based approach.[9] The Association agrees. Accordingly, we believe that any further study should consider whether an entity-based approach is appropriate or practical for investment funds, given their unique characteristics and regulatory structure. At the same time, consideration should be given to whether national sectoral enhancements would be more appropriate in the investment fund context. Finally, FSB and IOSCO should also consider the potential adverse impacts that their proposal could have on companies and markets, and the retirees and workers who invest in these funds.

The indicators that the FSB and IOSCO are asking for comments on could lead to the designation of investment funds that operate in the world's most established and heavily regulated markets while ignoring potentially problematic general sector-wide practices such designated funds may not be involved in. Instead of attempting to identify and single out investment funds based on size (or size in combination with other indicators), the FSB and

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[8] Document at 5.

[9] Document at 32.

IOSCO should instead study which sector-wide practices and market dynamics could potentially create a systemic risk to the financial system. After identifying these practices, each country's regulatory scheme should be examined to determine if the identified systemic risks are already addressed by the home country regulator. For example, if counterparty concentration is a potential source of systemic risk, do the rules related to OTC derivatives trading and clearing that are part of Title VII of the U.S. Dodd-Frank Act or those that are part of the European Market Infrastructure Regulation address these risks?

The Document expressly acknowledges that an activities-based approach to the investment fund sector could be an appropriate means of addressing any financial stability risk in the sector.[10] The Association believes that an activities-based approach is a more appropriate means of addressing financial stability in the investment fund sector as it would address conduct that may be undertaken by all investment funds, rather than just focusing on the conduct of the largest ones. In the U.S. registered funds context, we believe that activities-based requirements, such as maintaining high levels of liquid assets and limiting leverage, play an important role in mitigating against potential financial stability threats that might be associated with such funds. In addition, the Dodd-Frank Act implemented swap data reporting, swap clearing and execution requirements which mitigate the risk of contagion from a U.S. registered fund's exposure to its counterparties.

## 3. U.S. Registered Funds Cannot Reasonably Be Considered to Raise Systemic Risks

### A. There is no evidence to support an assertion that U.S. registered funds are subject to destabilizing runs.

U.S. registered funds do not raise, and historically have not raised, systemic risk concerns. Even during the financial crisis, the period of time giving rise to the G20's mandate to identify systemic risk, registered open-end funds did not experience runs. In September, October and November of 2008, the worst period of the financial crisis, registered U.S. non-money market funds experienced net redemptions of approximately $60 billion, $128 billion and $41 billion, respectively, on a net asset base of almost $5.8 trillion.[11] The fund industry returned to more historic trends in terms of flows of funds quickly; in January of 2009, funds experienced net purchases of shares totaling $25 billion.[12] This high level of stability even during an extraordinarily volatile period is a clear indication that investors in non-money market U.S. registered funds are long term investors who do not pose a material threat for runs. This point should play a critical role in any analysis of whether U.S. registered funds pose potential global systemic risk to financial stability.

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10 In this regard, the Document states, "[i]ndeed, another possible approach to assessing systemic risk in the asset management sector could be to consider possible financial stability risks that could arise out of certain asset management-related activities. Under this approach, the methodologies would consider how particular activities or group of activities might pose systemic risks." *See* Id.

11 *See* ICI, *Long-Term Mutual Fund Flows Historical Data* (2013), http://www.ici.org/info/flows data 2013.xls (regarding redemption activity); ICI, *2013 Investment Company Fact Book: A Review of Trends and Activity in the Investment Company Industry* 144 (2013), available at http://www.icifactbook.org/pdf.2013 factbook.pdf (regarding total assets) ("Factbook").

12 Factbook at 144.

## B. U.S. Registered Funds are not generators, creators or transmitters of risk.

U.S. registered funds are vehicles through which investors access investment markets. The risks inherent in those investments and markets already exist, having been created by entities that create risk in the ordinary course of their business. U.S. registered funds do not create similar risks. Indeed, to the extent that the risks created by others in the marketplace are reduced through increased systemic regulation, then it follows that investment funds would be operating in a more stable environment. As a result, it also follows that the risks they face and those they create or pass along would have been correspondingly reduced or mitigated. Any rigorous analysis of U.S. registered funds should consider not only the abstract risks that they create, but the extent to which the analysis would be impacted by variables such as increased regulation of the principal creators of risk in the markets.

Importantly, U.S. registered funds have numerous regulatory protections in place to prevent systemic impact on the financial system. As the Document recognizes, "funds contain a specific 'shock absorber' feature . . . . In particular, fund investors absorb the negative effects that might be caused by the distress or even the default of a fund, thereby mitigating the eventual contagion effects in the broader financial system."[13] The Document cites data that supports a conclusion that U.S. registered funds do *not* create a systemic risk in the event they should fail or be liquidated:

> According to relevant industry data for US mutual funds . . . from 2000 to 2012, on average 671 new funds were launched per year, compared to an average of 291 liquidations (and 296 mergers). Moreover, throughout the same period, mutual fund launches have outnumbered liquidations, except 2009, when liquidations were more numerous by a very narrow margin. ***In addition, even when viewed in the aggregate, no mutual fund liquidations led to a systemic market impact throughout the observation period.*** Part of the explanation may be that many US investors hold mutual fund shares for retirement purposes. As such, these investors' investment horizon could be long-term, whereby they would prefer to remain invested rather than cash-out during a market downturn.[14]

Even in the event of a run on a fund, asset managers have numerous tools available to mitigate any destabilizing impact of a run, as the Document points out:

> [A]sset managers may temporarily implement specific liquidity management tools such as swing-pricing, anti-dilution levies, redemption gates, side-pockets, redemptions in kind or temporary suspensions. Moreover, funds close (and are launched) on a regular basis with negligible or no market impact. In other words, the investment fund industry is highly competitive with numerous

[13] Document at 29.

[14] Document at 30 n. 38 (emphasis added).

substitutes existing for most investment fund strategies (funds are highly substitutable).[15]

We believe that the lack of adverse impact of U.S. registered funds on financial stability is attributable to (i) the long-term investment horizon of the savers and workers who invest their savings in such funds and (ii) the regulatory structure already governing the operation of these funds. In that regard the ICA limits the risks associated with funds by, among other things requiring funds to maintain a high level of liquid assets and limit their leverage and borrowing.

### C. The two transmission channels identified by the Document are already addressed by the regulatory structure that applies to U.S. registered funds.

The Document's grounds for considering investment funds as G-SIFIs is based on only two purported systemic risk transmission channels: (i) "exposures/counterparty channel" risk; and (ii) "asset liquidation/market channel" risk. These risks are specifically accounted for by the U.S regulatory system.[16] The Document does not provide empirical or other support for attributing these purported risk transmission channels to investment funds. Given the negative financial and competitive impacts that designation as an NBNI G-SIFI can have on companies, a decision to treat investment funds as a category of NBNI entities that could be designated as NBNI G-SIFIs must be based on a stronger foundation.

Even if these risks were supported by any kind of data or analysis, the U.S. regulatory structure already adequately addresses them. As explained in more detail below, exposure and counterparty channel risk is mitigated by the fact that U.S. registered funds must have 300% asset coverage for any borrowings undertaken, and, even in the case of the use of derivatives, must segregate or earmark assets to cover the exposure to the counterparty. Moreover, as previously discussed recent changes to the derivatives markets under the Dodd-Frank Act have reduced counterparty risk through central clearing requirements[17] and, in some cases, mandated swap facility execution requirements.[18]

Asset liquidation and market channel risk is also addressed in the U.S. regulatory system for investment funds. U.S. registered funds have measures in place to satisfy redemption requests and mitigate the effect of any rapid redemptions on other market participants. Under the U.S. regulatory regime, U.S. registered funds must have 85% of their portfolio in liquid assets. Furthermore, it is common for funds to enter into liquidity facilities with banks to cover rapid redemption requests in times of emergency. The practical effect of these liquidity facilities is that funds can borrow from a syndicate of banks to meet their redemption requests in cash, and then sell the underlying assets when the market is more favorable to that asset. This prevents large U.S. registered funds from dumping assets into the market and also prevents market freezes

[15] Document at 30.

[16] Again, this is why it is essential that an investment fund's home country regulatory scheme should be taken into account in both an evaluation of whether investment funds in general should be viewed as a category from which potential NBNI G-SIFIs could be drawn and whether any particular investment fund should be designated as an NBNI G-SIFI.

[17] *See* 15 U.S.C. § 78c-3(a)(1) (as added by section 763 of the Dodd-Frank Act).

[18] 15 U.S.C. § 78q-1(i).

thereby severely limiting their effect on other market participants and keeping systemic risk to a minimum.

### D. Concerns about counterparty exposures to U.S. registered funds are unfounded.

U.S. registered funds are not sources of counterparty risk. The ICA and SEC guidance require a registered open-end fund to maintain liquid assets to cover 100% of the fund's obligation under a contract with an obligation to pay in the future for consideration already received (including short transactions and derivatives), which must be marked to market daily. This ensures that such a fund always has adequate assets to meet obligations arising from these types of transactions. In another example of activities-based regulation, derivatives are increasingly moving to centrally-cleared exchanges, which reduce counterparty risk. Moreover, most U.S. registered funds trade only with counterparties that meet both internal and external credit rating requirements.

## 4. Any Entity-Based Process Should Consider Risk-Mitigating Factors and the Adverse Impacts that Systemic Regulation Can Have

Should the FSB decide to use an entity-based approach versus a more appropriate activities-based approach, any consideration of designating a particular investment fund should expressly account for factors that may mitigate against it being a systemic risk. Mitigating factors that should be considered in regard to any potential NBNI G-SIFI designation should include: (i) the capability of management, (ii) risk controls, (iii) board/governance oversight, (iv) asset diversification, (v) liquidity options, (vi) disclosures to investors, (vii) substitutability and (vii) the relative ease of resolvability.

As discussed earlier, the FSB should also consider the investment fund's home country regulatory environment and the capabilities of the home country regulator. With these factors in mind, the Association would like to point out that the ICA and the SEC's rules and guidance thereunder provide a robust regulatory regime that has been remarkably effective in both providing material information to investors and potential investors, as well as mitigating the risks to investors and the financial system of financial difficulties experienced by a U.S. registered fund, up to and including a liquidation of the fund.

To the extent that the FSB and IOSCO determine to proceed with the proposed Investment Fund Methodology, we believe that it is essential that any consideration of a particular U.S. registered fund for NBNI G-SIFI designation expressly include the foregoing risk-mitigating factors.

The Document does not take into consideration that the actions proposed to do so could themselves have greater costs than benefits, or could in fact disturb the equilibrium of markets in a way that actually creates more risk and increases the chances of global financial distress. It is problematic to assume that risk mitigating tools applied to individual companies will make markets safer and more systemically stable, and this issue is magnified when the analysis does not also rigorously consider how the purported improvements in regulation may, in fact, negatively impact investors, companies, competition and global systemic risk.

The Document does not indicate what type of policy measures the FSB and IOSCO might ultimately seek to apply to investment funds that are designated as NBNI G-SIFIs. We believe, however, that imposing special requirements on U.S. registered funds selected because of their size will ultimately disadvantage those funds which will directly harm the savers, workers and retirees that have entrusted their savings to these investment vehicles. As a practical matter, policy measures designed by the FSB and IOSCO could adversely affect the viability of these funds and their ability to continue to serve the investment objectives of savers and retirees. Such policy measures could impose additional costs on NBNI G-SIFI designated funds, or subject them to restrictions that will diminish their ability to compete with investments that are not designated as NBNI G-SIFIs and thereby adversely impact the shareholders of designated funds.

**5. U.S. Asset Managers Do Not Reasonably Raise Systemic Risks**

The Association notes that the Document identifies asset managers as a possible type of entity to be separately considered as NBNI G-SIFIs. The Association wishes to express its opposition to adding or conjoining asset managers as part of such a designation process for the reasons discussed below.

The asset management business does not create the type of systemic risks that the G20 mandated the FSB and IOSCO to assess. The nature of the asset management business makes it fundamentally different than banks and other type of financial entities. It is important to note that investors bear the risk if an investment fund fails and not the asset manager. The activities of asset managers who are investing client assets in accordance with client guidelines and return objectives do not create the potential for systemic risk that the activities of financial institutions who act as a principal or invest their own assets do.

First, asset managers are not at risk of failure because they do not invest their own balance sheet assets. Second, even in the situation of the failure of an asset manager, such an event would not cause a disorderly failure of a fund because the assets do not belong to the asset manager. They belong to the asset manager's clients and are not commingled with asset manager assets and the creditors of the asset manager cannot reach client assets. Client assets are generally held by a separate custodian that is selected by the client and are subject to regulatory protections.

Investment funds are generally substitutable. The asset manager's failure has no impact on the investment fund and its assets and does not cause a liquidation of a fund. The investment fund client of a failed asset manager could easily migrate to another asset manager with few transition costs given the large and diffuse nature of the asset management industry. Such a transition would generally not result in the sale or liquidation of any assets and therefore would not present the potential for systemic risk to the financial system that could result from "fire sales" during a market crisis. An asset manager's provision of investment advisory services for a U.S. registered fund is performed on a contractual basis which is approved by the fund's board of directors under a rigorous review process. Should an asset manager fail, the investment fund (which is a separate entity apart from the asset manager) would contract with a new, solvent asset manager. Historically, even in situations where a fund's board decided to liquidate the investment fund instead of hiring a new asset manager, such actions have not caused a systemic effect. In fact, as the Document points out, "even when viewed in the aggregate, no mutual fund liquidations led to a systemic market impact" throughout 2000 to 2012.[19]

Bank-like prudential standards are not applicable, meaningful or appropriate in the context of an asset manager. Asset managers, in that capacity, do not engage in activities in which they commit their own capital, and do not borrow or issue debt to finance such balance sheet activities. Asset managers simply act on behalf of their clients, managing client assets for a fee. Importantly, institutional asset managers do not act with their own short-term interests at heart. Instead, they act with the goal of establishing consistent, long-term returns designed to build trust in their ability to produce a meaningful return on their investments. To that end, asset managers should not be part of the assessment methodologies because there is simply no foundation to include them.

## 6. U.S. Activities Based Regulation Is a More Effective Means of Regulating Perceived Fund Risks

Instead of using an entity-based approach the FSB and IOSCO should follow an activities-based approach. The regulatory scheme governing U.S. registered funds results in these funds having many features that mitigate the possibility of disruptive mass redemptions. As explained above, U.S. investment funds are generally required to maintain 85% of their assets in liquid securities under SEC guidance. They are also subject to strict limitations on their ability to utilize leverage which argues against the concern expressed in the Document that leverage may amplify risks to an investment fund or the markets in which it participates in the remote event of a run or distress.

The U.S regulatory scheme also requires in most circumstances that U.S. registered funds use a floating NAV. Through this requirement and through required disclosure that investing in a fund comes with the risk of losing money, investors understand and are accustomed to periodic increases or decreases in fund NAV. This understanding, and the fact that funds mark-to-market their assets daily, helps to protect against runs by eliminating any first-mover advantage. Moreover, U.S. activities-based regulation provides funds with the tools to respond to unusual market conditions, including: (i) postponing payment of redemptions when the market is closed; (ii) suspending redemptions in the event of an emergency (with the SEC's concurrence); and (iii) generally reserving the right to redeem in kind. An activities-based approach is better suited for the investment fund industry than the entity-based approach proposed in the Document. The current proposed entity-based approach to investment funds would negatively impact investors by taking away the benefits of economies of scale and would lead to unfair market advantages for undesignated funds in terms of cost.

## 7. Conclusion

The Association thanks the FSB and IOSCO for the opportunity to comment on the Document and appreciates their efforts in seeking to address financial stability and their focus on systemic risk issues. As outlined in our letter, the Association does not believe that designating investment funds or asset managers is an effective or appropriate means of addressing potential

[19] Document at 30 n. 38

systemic risk. We think that a more effective and appropriate undertaking would be for the FSB and IOSCO to focus on data collection and analysis, with a goal of identifying market-wide activities that could contribute to systemic risk. The Association welcomes the opportunity to further discuss the concerns and recommendations we raised in this letter. If you have any questions, please do not hesitate to contact the undersigned at jgidman@loomissayles.com or (617) 748-1748.

On behalf of the Association of Institution INVESTORS,

John R. Gidman