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September 21, 2016

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

Submitted via e-mail to: fsb@fsb.org

Re: **Consultative Document: Proposed Policy Recommendations to Address Structural Vulnerabilities from Asset Management Activities dated June 22, 2016**

Dear Sirs/Madams:

Fidelity Management & Research Company[1] ("Fidelity") appreciates the opportunity to comment on the *Consultative Document, Proposed Policy Recommendations to Address Structural Vulnerabilities from Asset Management Activities* (the "Consultative Document"), published by the Financial Stability Board ("FSB") on June 22, 2016.[2]

Over two years have passed since the FSB published its initial proposal for assessing the asset management industry in search of hypothetical threats to the global financial system.[3] Industry participants, including Fidelity, filed numerous comment letters on the First Consultative Document. Commenters advised the FSB that the proposed methodology for designating large investment funds as "Global Systemically Important Financial Institutions" ("G-SIFIs") was flawed because it failed to demonstrate that funds or managers threaten global financial stability, failed to recognize that G-SIFI designation, intended for banks, is an inappropriate policy tool for regulating fundamentally different asset management entities, and focused primarily on size, which is not positively correlated with potential systemic risk in asset management the way it is in banking.[4] Fidelity, among others, recommended that the FSB and

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[1] Fidelity and its affiliates are leading providers of mutual fund management and distribution, securities brokerage, and retirement recordkeeping services, among other businesses.

[2] Fin. Stability Bd., Consultative Document: Proposed Policy Recommendations to Address Structural Vulnerabilities from Asset Management Activities (June 22, 2016), *available at* http://www.fsb.org/wp-content/uploads/FSB-Asset-Management-Consultative-Document.pdf (hereinafter the "Consultative Document").

[3] Fin. Stability Bd. & Int'l Org. of Sec. Comm'ns, Consultative Document: Assessment Methodologies for Identifying Non-Bank Non-Insurer Global Systemically Important Financial Institutions (Jan. 8, 2014) (hereinafter, the "First Consultative Document"), *available at* http://www.fsb.org/wp-content/uploads/r_140108.pdf.

[4] *See, e.g.*, Letter from Scott C. Goebel, Senior Vice President & Gen. Couns., Fidelity Mgmt. & Res. Co. to Secretariat of the Fin. Stability Bd., at 14 (April 7, 2014) (hereinafter, "Fidelity-FSB 2014 Letter"), *available at* http://www.fsb.org/wp-content/uploads/r_140423s.pdf; Letter from Paul Schott Stevens, President & CEO, Investment Company Institute to the Secretariat of the Fin. Stability Bd., 6 (Apr. 7, 2014) (hereinafter, "ICI-FSB

IOSCO instead conduct a balanced review of asset management products and activities that accounts for the ways in which they enhance financial stability and economic growth, places the potential risks posed by investment funds and their asset managers in proper context among risks posed by the diverse array of asset owners and capital markets participants, and recognizes the mitigating effects of existing regulations, contract terms and economic incentives. We reiterated these recommendations in our response[5] to the FSB's Second Consultative Document published in March 2015.[6]

We are pleased that the FSB has shifted its approach in the latest Consultative Document to focus on certain asset management products and activities, rather than individual entities, and to consider whether such activities create risks that are not already mitigated.[7] We appreciate the work required to make this shift and the significant amount of work to be done to pursue this course. We believe that any future work by the FSB or IOSCO should continue to follow this approach and we stand ready to continue to engage with the regulators in these efforts. We commend the FSB and IOSCO for continuing their fact gathering exercise, because up to this point, the FSB, ESRB, FSOC and other similar bodies have too often based their systemic risk assessments and resulting policy recommendations on hypotheticals, rather than data and analysis.[8]

We believe that the Consultative Document makes good progress in many respects. However, if the FSB and IOSCO make policy recommendations in the future concerning the asset management industry, they should be based on sound data and economic analysis that is

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2014 Letter"), *available at* http://www.financialstabilityboard.org/wp-content/uploads/r_140423af.pdf; Letter from Barbara Novick, Vice Chairman, BlackRock, Inc. to the Secretariat of the Fin. Stability Bd., 1 (Apr. 7, 2014), *available at* http://www.financialstabilityboard.org/wp-content/uploads/r_140423h.pdf.

[5] *See* Letter from Scott C. Goebel, Senior Vice President & Gen. Couns., Fidelity Mgmt. & Res. Co. to Secretariat of the Fin. Stability Bd., at 23-25, 32 (May 27, 2015) (hereinafter, "Fidelity-FSB 2015 Letter"), *available at* http://www.fsb.org/wp-content/uploads/Fidelity-Management-and-Research-Company.pdf.

[6] Fin. Stability Bd. & Int'l Org. of Sec. Comm'ns, Consultative Document (2nd): Assessment Methodologies for Identifying Non-Bank Non-Insurer Global Systemically Important Financial Institutions (Mar. 4, 2015) (hereinafter, the "Second Consultative Document"), *available at* http://www.fsb.org/wp-content/uploads/2nd-Con-Doc-on-NBNI-G-SIFI-methodologies.pdf.

[7] As we explained in the Fidelity-FSB 2015 Letter and other commenters explained in their respective letters, the effort to design a G-SIFI methodology for funds or their managers is irredeemably flawed and should be abandoned permanently.

[8] *See e.g.*, Investment Company Institute Letter to Fin. Stability Oversight Council, at 6 (July 18, 2016) (hereinafter, "ICI-FSOC 2016 Letter"), *available at* https://www.ici.org/pdf/16_ici_fsoc_ltr.pdf (criticizing recent FSOC report on the asset management industry and noting concerns raised about destabilizing effect of "forced" asset sales is the same faulty hypothesis previously argued by the OFR and FSB); Fidelity-FSB 2014 Letter, at 11 (FSB fails to define key terms such as "significant disruption," "wider financial systems" and "economic activity"); Fidelity-FSB 2015 Letter, at 15 (noting the Second Consultative Document uses the words "may," "might," "could," "potential" and "potentially" an astounding 402 times in the course of the 57 page report); *see also* Letter from Scott C. Goebel, Senior Vice President & Gen. Couns., Fidelity Mgmt. & Res. Co. to U.S. Securities & Exchange Commission, at 7 (November 1, 2013), *available at* https://www.sec.gov/comments/am-1/am1-19.pdf (responding to Office of Financial Research Report entitled "Asset Management and Financial Stability" noting that the "OFR makes many broad, unsubstantiated statements without clearly defining the issues, scope, or scale, and implies that a hypothetical occurrence may somehow be risk worthy of the FSOC's attention no matter how improbable.").

published for review and comment before policies are finalized. As we will discuss in more detail, the FSB should conduct an economic analysis to determine whether any material threats to global financial stability exist and whether potential policy responses would do more good than harm in addressing them. With respect to U.S. open-end funds[9] and their managers, any final recommendations should reflect, or at least accommodate, final rulemakings underway by the U.S. Securities and Exchange Commission ("SEC"). We also remain concerned that several faulty premises persist concerning the asset management industry and the mutual fund business in particular. These include the following issues, which we discuss in more detail:

1. The FSB still has not presented data or empirical analysis demonstrating that open-end funds or fund managers threaten the stability of the global financial system; rather, the recommendations are based on conjecture regarding hypothetical risks and "structural vulnerabilities", a flaw exacerbated by the failure to define key terms in the Consultative Document. Nor has the FSB responded to the substantial evidence that open-end funds or fund managers are not a source of systemic risk.

2. The Consultative Document perpetuates flawed hypotheses concerning mutual fund liquidity and redemptions, including alleged "first-mover" advantages, "runs" on variable net asset value funds, the existence of "spillover effects" to the financial markets that are large enough to damage the global economy, and the purported existence of "liquidity mismatches" in open-end funds that constitute a "structural vulnerability", which despite existing over the past 75 years has never threatened global financial stability.

3. The Consultative Document discusses some, but not all, of the existing mitigants to the alleged structural vulnerabilities. For example, tools that fund managers have at their disposal to manage redemption activity during stressed conditions, as well as regulations, contractual and retirement plan restrictions that affect redemptions, and economic incentives that provide disincentives for retirement account investors to withdraw their assets early, were omitted from the discussion.

4. The Consultative Document inappropriately transposes issues that may be experienced by a very small subset of open-end funds holding less liquid assets to the entire asset management industry. Even assuming that these issues are relevant to the entire subset of funds holding less liquid assets, those risks are immaterial to global financial stability.

5. The Consultative Document improperly equates idiosyncratic operational risk to global systemic risk. There is no nexus between operational risk at an asset manager and the stability of the global financial system. Conversely, there is no

[9] Under U.S. laws and regulations, the term "mutual fund" encompasses both open-end funds and money market funds. An exchange-traded fund is an open-end fund, but not a mutual fund. We use the term "open-end fund" to refer to all mutual funds and exchange-traded funds.

evidence that financial market stress causes or exacerbates operational risk in asset management.

6. Collective investment funds and professional management create significant economic and financial stability benefits that are widely acknowledged. The FSB fails to consider whether they would be reduced or altered by the policy recommendations in the Consultative Document.

I. Any Future FSB and IOSCO Policy Recommendations Should Be Based on Data and Economic Analysis Published for Review and Comment That Determines Whether Asset Management Activities Present Material Threats to Global Financial Stability That Warrant Additional Policy Responses.

If the FSB and IOSCO make policy recommendations in the future concerning the asset management industry, they should be based on sound data and economic analysis that is published for review and comment before policies are finalized. Similar to the analysis required of SEC rulemaking, the FSB should conduct its own economic analysis to determine whether any material threats to global financial stability exist and whether potential policy responses would do more good than harm in addressing them. If new policies are recommended, they should be sufficiently flexible to allow for differences among jurisdictions. With respect to U.S. funds and their managers, any final recommendations should reflect, or at least accommodate, final SEC rulemakings. This approach will ensure that FSB and IOSCO policies are not inconsistent with U.S. asset management and market regulations or the requirements of U.S. administrative law, which requires an economic analysis to support fair and reasoned decision making prior to the introduction of additional regulation. This will also protect against potential conflicts between global market regulations and U.S. rulemaking which could force asset managers to "face the impossible task of balancing their fiduciary duties to their clients and investors with regulatory obligations to do what is best for the financial system as a whole."[10]

We direct the FSB to the comprehensive rulemaking effort underway by the SEC with respect to U.S. mutual funds and advisers that addresses many of the same points as the Consultative Document.[11] Since December 2014, the SEC has issued proposed rules for the asset management industry addressing liquidity risk management,[12] the use of derivatives,

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[10] Remarks of SEC Commissioner Michael S. Piwowar Before the Quadrilateral Meeting of the FMLC/FMLG/FLB/EFMLG (July 20, 2016), *available at* https://www.sec.gov/news/speech/speech-piwowar-2016-07-20.html.

[11] *See* Keynote Address, SEC Regulation Outside the United States "The SEC at Home and Abroad," Andrew J. Donohue, Chief of Staff, InvestoRegulation Conference London (June 28, 2016), *available at* https://www.sec.gov/news/speech/andrew-donohue-investoregulation-conf-london.html ("Of course, our ability to effectively address issues abroad is not unrelated to our ability to be productive at home. And in that regard, the Commission has been firing on all cylinders").

[12] *See* Open-End Fund Liquidity Risk Management Programs; Swing Pricing; Re-Opening of Comment Period for Investment Company Reporting Modernization Release, Release Nos. 33-9922, IC-31835 (Sept. 22, 2015), 80 Fed. Reg. 62275 (Oct. 15, 2015), *available at* https://www.sec.gov/rules/proposed/2015/33-9922.pdf.

including measures to limit the amount of leverage funds can obtain through these instruments,[13] modernization of data reporting and disclosure by funds and advisers,[14] and business continuity and transition planning requirements.[15] Although we have provided comments to the SEC recommending improvements to certain aspects of their proposed rules, we are generally supportive of the proposed rules and continue to believe that the SEC, as the primary U.S. regulator, should lead rulemaking efforts affecting the U.S. asset management industry and play a leading role in related global initiatives.

The extensive U.S. rulemaking that is currently underway is given short shrift in the Consultative Document.[16] It does not contain any detailed discussion of these initiatives, the comments received on them, their applicability outside of the U.S., or their likely efficacy in addressing risks that the FSB contends threaten global financial stability. We note in particular that, before introducing any new rulemaking, the SEC must assess the costs and benefits of the intended regulation, and adopt it only upon a reasoned determination that the rule's benefits justify its cost.[17] This analysis includes a review and explanation of why the new regulation is "necessary or appropriate in the public interest" and whether it "will promote efficiency, competition, and capital formation."[18]

As the SEC observed, "[h]igh-quality economic analysis is an essential part" of its rulemaking as it "ensures that decisions to propose and adopt rules are informed by the best available information about a rule's likely economic consequences, and allows the Commission to meaningfully compare the proposed action with reasonable alternatives, including the alternative of not adopting a rule. The Commission has long recognized that a rule's potential benefits and costs should be considered in making a reasoned determination that adopting a rule

[13] *See* Use of Derivatives by Registered Investment Companies and Business Development Companies, 80 Fed. Reg. 80884 (Dec. 28, 2015), *available at* https://www.gpo.gov/fdsys/pkg/FR-2015-12-28/pdf/2015-31704.pdf.

[14] *See* Investment Company Reporting Modernization, Investment Company Act Release No. 31610 (May 20, 2015), 80 Fed. Reg. 33590 (June 12, 2015), *available at* https://www.sec.gov/rules/proposed/2015/33-9776.pdf.

[15] *See* Adviser Business Continuity and Transition Plans, 81 Fed. Reg. 43530 (July 5, 2016), *available at* https://www.gpo.gov/fdsys/pkg/FR-2016-07-05/pdf/2016-15675.pdf.

[16] The Consultative Document references, in the vaguest of terms the other "regulatory" initiatives that may exist, but provides no analysis of any of these initiatives to determine whether residual risks may persist. This is a baseline review that must be conducted by the FSB prior to any further issuances of recommendations. *See* Consultative Document, at 11, 23, 29 (referencing, without specificity that "regulatory frameworks generally restrict" holding of illiquid asses, a "number of regulatory measures" with respect to leverage, and a "number of regulatory tools and market practices").

[17] *Motor Vehicle Mfrs. Ass'n of U.S., Inc.* v. *State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983) (under U.S. law, an agency must "articulate a satisfactory explanation for its action" that draws "a rational connection between the facts found and the choice made.").

[18] 15 U.S.C. 78c(f) (2006). Thorough economic analysis is also a pre-requisite for new proposals under EU law, just as it is under U.S. law. *See* Consultation Document, Review of the EU Macro-Prudential Policy Framework, at 11, *available at* http://ec.europa.eu/finance/consultations/2016/macroprudential-framework/docs/consultation-document_en.pdf ("A thorough analysis and detection of potential new risks stemming from more market-based finance is prerequisite in order to support the establishment of new macro-prudential instruments in EU law.").

is in the public interest."[19] Conjecture is an insufficient basis to justify new policies at the U.S. national level.[20] We believe that a stronger foundation should be established for policy recommendations outside of the U.S., especially for policies that are intended to be applied globally, including to entities in the U.S.

II. The Consultative Document Does Not Define Key Terms, Relies on Conjecture and Fails to Provide Empirical Evidence for Many of the FSB's Conclusions and Recommendations or to Respond to Empirical Evidence that Open-End Funds and Managers Do Not Present Systemic Risk.

The Consultative Document fails to define or quantify key terms that underlie the FSB's policy recommendations. For example, important terms such as "financial stability," "material liquidity mismatches," "stressed market conditions," "extraordinary liquidity risk management tools," "negative spillovers" and "critical services" are nowhere defined or measured in the Consultative Document. Vague terms unaccompanied by empirical evidence simply do not establish the necessary framework to determine whether asset management activities contribute to global systemic risk or to design effective and efficient policies to mitigate such a risk.

As the Nobel laureate Lars Peter Hansen observes when discussing systemic risk regulation, the "know it when you see it approach" invites "a substantial amount of regulatory discretion," which can "lead to bad government policy, including the temptation to respond to political pressures" rather than economic evidence.[21] Professor Matthew Richardson similarly has observed that, "[i]n order to regulate and manage systemic risk, one must be able to measure systemic risk. And in order to measure systemic risk, one needs to be able to define what it is."[22] In his paper, Professor Richardson clearly defines the source of systemic risk and a framework that would enable the creation of objective metrics to measure it. We recommend the FSB pursue such an empirical approach.

Rather than relying on empirical evidence, the basis for the FSB's conclusion that "financial stability risks" exist in the investment management industry is mired in hypothetical "*ifs*" based on events that "*could*" occur, but viewing actual historical precedent, have *never* occurred.[23] This same type of speculation existed in the FSB's prior consultative reports[24] and it

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[19] *See* U.S. Securities & Exchange Commission, Current Guidance on Economic Analysis in SEC Rulemakings, at 1 (Mar. 16, 2012), *available at* https://www.sec.gov/divisions/riskfin/rsfi_guidance_econ_analy_secrulemaking.pdf.

[20] In the United States, "speculation is an inadequate replacement for" an agency's "duty to undertake an examination of the relevant data and reasoned analysis." *Horsehead Res. Dev. Co., Inc. v. Browner*, 16 F.3d 1246, 1269 (D.C. Cir. 1994).

[21] Lars Peter Hansen, Challenges in Identifying and Measuring Systemic Risk, at 16 (Feb. 11, 2013), *available at* http://www.nber.org/chapters/c12507.pdf.

[22] Matthew Richardson, Prof. of Applied Econ., NYU Stern Sch. Of Bus., Asset Management and Systemic Risk: A Framework for Analysis, at 5 (Mar. 19, 2015) (on file with the Fin. Stability Oversight Council, Docket No. FSOC 2014-0001), *available at* https://www.regulations.gov/document?D=FSOC-2014-0001-0033.

[23] *See* Consultative Document, at 4 ("*If* market prices were to drop sharply and liquidity were to deteriorate, investors in less liquid asset classes through open-ended funds *could* experience greater and more sudden losses than expected, which *could* result in a significant number of fund investors attempting to exit these asset classes at the

does not appear that any effort has been made since to test and reexamine these hypotheses to determine whether they are correct and should serve as the basis for new policies. The FSB's recommendations are even less persuasive since they continue to advance the same hypothetical scenarios argued in its prior consultative documents[25] thereby ignoring the compelling empirical evidence presented by Fidelity and many others that mutual funds do not create or amplify systemic risk. Academic research and empirical evidence show that concerns over alleged "first mover advantages," investor "herding" and the risk of asset "fire sales" [26] have not materialized and are unlikely to do so in the future in mutual funds of any size, thereby contradicting the FSB's hypothesis that these dynamics exist and threaten the stability of the global financial system. In addition, the FSB has acknowledged that both funds and managers close regularly with no systemic impact,[27] in contrast to the notion that a fund or manager could fail in a disorderly fashion and threaten global financial stability.

No Demonstrated First-Mover Advantage. As Professor Matthew Richardson has explained, "in a setting in which assets are fairly priced by funds with floating NAVs, it is not

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same time. The action of these fund investors *could* amplify downward repricing of assets and increase the severity of liquidity strains in the affected asset classes. It *could* also increase the potential for contagion across asset classes.") (Emphasis added); *see also id.* at 14 ("There are a *number of contingencies* that would need to occur for the liquidity transformation in open-ended funds to have an amplifying effect on risks to financial stability. There *would* need to be significant redemptions from funds (and greater redemptions than would be the case if investors had invested directly in the markets) accompanied with significant asset sales by those funds (particularly sales of less liquid assets). *Finally*, those asset sales would need to be significant enough, either relative to total assets or normal trading volume in particular market segments, to lead to material price declines or increases in price volatility in the secondary markets that would be serious enough to impair market access by borrowers. *Furthermore*, when myriad market participants sell assets, the amplification can become more acute when it also prompts leveraged investors (e.g. hedge funds, banks, broker-dealers) to unwind risk positions in markets. *If* this occurred, it *could* affect other financial institutions and the ability of corporations and sovereigns to raise money in the capital markets and subsequently *could* spill over to the real economy.") (Emphasis added).

[24] *See supra* note 8. Fidelity and other commentators highlighted the hypothesis in their response to the Second Consultative Document and the FSB in the latest report again offers no data or analysis that supports its hypotheses or answers rebuttals of those hypotheses.

[25] Second Consultative Document, at 31 ("forced liquidation of an investment fund . . . *could* have a destabilizing impact"); *id.* at 32 ("exposure/counterparty channel involves impact that the distress or liquidation of an investment fund *could* have on other market participants"); *id.* at 33 ("With respect to open-end funds, investors *could* have an incentive to redeem before other investors"); *id.* at 33 (large funds' abrupt sales *could* cause distortions); *id.* at 34 ("In sum, an individual investment fund *could* have the capacity under certain circumstances to exert downward pressure on the market prices of assets"); *See also* Letter from Scott C. Goebel, Senior Vice President & Gen. Couns., Fidelity Mgmt. & Res. Co. to the Fin. Stability Oversight Council at 5-12 (Mar. 25, 2015), *attached as Appendix B* to the Fidelity-FSB 2015 Letter (hereinafter, the "Fidelity-FSOC 2015 Letter"); Letter from Paul Schott Stevens, President & CEO, Investment Company Institute to the Fin. Stability Oversight Council, at 10-49 (Mar. 25, 2015) (hereinafter, "ICI-FSOC 2015 Letter."), *available at* http://www.ici.org/pdf/15_ici_fsoc_ltr.pdf.

[26] Consultative Document, at 10-12.

[27] *See* Consultative Document, at 8 ("Given that an asset manager's balance sheet is generally very small relative to the size of assets managed, distress at the level of the asset manager should generally pose less of a risk to the financial system than distress across its funds."); First Consultative Document, at 30, n. 38 ("[E]ven when viewed in the aggregate, no mutual fund liquidations led to a systemic market impact throughout the [2000-2012] 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.").

apparent why mutual fund investors are more likely to redeem (*i.e.*, leading to asset sales) than other investors in those assets."[28] Even if there were small temporary lags or discrepancies in pricing an individual fund's shares, it is unrealistic to assert that these would be widespread across funds[29] or that most mutual fund investors, who are predominately individuals saving for retirement and other long-term goals, would consider them material.[30] Further, the first-mover advantage hypothesis is countered by the inherent characteristics of mutual fund portfolio and share pricing requirements and prudent liquidity management policies. Mutual funds have variable net asset values and mark the value of their underlying assets to market daily. As a result, redeeming investors receive only the current market value of their investments, determined *after* the investor makes a redemption request and generally by the end of the trading day.[31] If redeeming investors are unaware of the price they will receive when they redeem, and existing liquidity management policies require sufficient liquidity exists to meet such redemptions, by definition there can be no "first-mover" advantages.[32] If there were a first-mover advantage, one would expect to see a spike in redemptions during market stress. Precedent shows that, even in times of extreme distress in the financial markets, the maximum monthly outflows for investors in U.S. equity mutual funds constituted less than four percent of all U.S. fund assets, and the maximum monthly outflows for investors in U.S. bond mutual funds constituted less than ten percent of U.S. fund assets.[33]

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[28] Richardson, *supra* note 22, at 20.

[29] *See id.* at 32 ("There is nothing to suggest that large funds are more susceptible to redemption risk than smaller funds or more prone to run-like behavior on the part of investors. In fact, because we are comparing two groups of mutual funds with roughly the same total AUM, this result implies that fire sales are not any more of an issue for large funds than the rest of the mutual fund sector. Not only is there no indication of run-like behavior, but there is no evidence of any difference between large funds and the rest of the mutual fund sector with respect to flows.").

[30] *See* ICI-FSB 2014 Letter, at 5 (stating that "across a range of adverse market events and conditions, sales of stocks and bonds by regulated US funds represent a modest share of overall market activity—a fact that reflects the nature today of their largely retail investor base and the long-term financial goals of most fund investors"). *See also* Fidelity-FSOC 2015 Letter, at 8-12.

[31] *See also* Fidelity-FSOC 2015 Letter, at 3 (refuting "first-mover" advantage since redemption requests are processed at the share price next determined after transaction requests are received by a fund, which prevents investors from engaging in price arbitrage. Mutual funds must disclose their NAVs each day and must frequently disclose their holdings); *see also id.* at 8-12 (demonstrating immateriality of any alleged first-mover advantage created by net outflows in the poorest performing illiquid equity mutual funds that are not held through retirement share classes, at 2% of assets compared with outflows of approximately 0.75% in similarly performing funds holding more liquid securities); *see also* ICI-FSOC 2016 Letter, at 3, Appendix B (explaining that concerns about first-mover advantage are unfounded since (i) existing regulatory and characteristics of mutual funds serve to restrict severely any benefit to "early" redeeming investors and mitigate the impact to remaining investors, and (ii) argument that mutual funds sell most liquid assets first to meet redemptions does not accurately describe how mutual funds manage liquidity as evidenced by data showing that short-term asset ratios, even among mutual funds holding less liquid assets, do not deteriorate much if at all in response to net cash outflows).

[32] *See* Fidelity-FSOC 2015 Letter, at 6 (detailing numerous mechanisms at portfolio managers' disposal to meet redemption demands).

[33] ICI-FSB 2014 Letter, at F4-F10 (data reflecting that during average market conditions from 1985 to 2013 monthly flows cluster around zero and during highly stressed market conditions (including the October-December 1987 stock market crash and recent 2007-2009 financial crisis) there was a small increase in outflows with the majority of equity mutual funds experiencing less than 6 percent outflow of assets).

No Investor "Herding" Risk. The FSB's hypothesis of investors in traditional variable NAV mutual funds (*e.g.*, non-money market funds) causing systemic risk during market downturns by behaving similarly presumes that investors only engage in one-way selling. This assumption ignores empirical evidence showing that investors *purchase* as well as *sell* shares, the net result that during historical periods of market stress, trading volumes frequently rise.[34] The FSB also presents no empirical evidence that investor "herding" exists or that it is magnified among mutual fund investors. To the contrary, "the mutual fund industry has never experienced the harmonized and sizeable redemption behavior associated with the 'Herding' theory and its implied systemic risk" [35] and the FSB has not provided data to otherwise support its conclusion.

No "Fire Sales" Risk. There is also no history of mutual fund "fire sales" causing global financial problems, even in the asset classes that most concern the FSB, such as high yield bond funds.[36] Mutual funds can use a wide array of liquidity management tools to avoid selling assets at steep discounts. Among other things, funds can use cash holdings, investor inflows, maturing securities, interest payments, and lines of credit, manage asset sales to minimize their impact, pay redemption requests in securities, or delay redemption payments for up to seven days.[37] Even if during these stressed periods "fire sales" of U.S. mutual fund assets were to occur, they would be unlikely to have a significant impact on market prices because the sales of portfolio securities by U.S. mutual funds are a small portion of overall market trading volume.[38] Indeed, as Professor Richardson explains, since fire sales depend on the redemption behavior of a fund's investors relative to other investors, given the structural differences between mutual funds and other potential holders of financial assets – such as lower levels of leverage, limited funding needs, liquidity requirements, and no access to central bank safety nets or governmental support – there is no evidence that mutual funds pose equivalent, let alone greater, problems from the standpoint of systemic risk."[39]

Fund and Manager Closures Do Not Create Systemic Risk. Limits on leverage that mutual funds can employ effectively eliminate the possibility they will "fail" in any plausible scenario, let alone in a disorderly fashion that threatens global financial stability.[40] Both the

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[34] *See* ICI-FSOC 2016 Letter, at B-2.

[35] Gaston Gelos, International Mutual Funds, Capital Flow Volatility, and Contagion - A Survey, IMF Working Paper, at 9 (2011), *available at* http://www.imf.org/external/pubs/ft/wp/2011/wp1192.pdf ("a look from an aggregate perspective already reveals that any simplistic characterization of the behavior of [mutual] funds is likely to be misleading; while there is volatility both at the level of the flows in [and] out of these as well as in the funds' movements in and out of countries, emerging market funds do not move in tandem as a single herd.); *see also* Letter from Avi Nachmany, Director of Research, Strategic Insight to the Fin. Stability Oversight Council, at 4 (Mar. 23, 2015), *available at* https://www.regulations.gov/document?D=FSOC-2014-0001-0016.

[36] *See* ICI-FSOC 2015 Letter, at 35 (data showing during period of increased net outflows of high-yield bond funds from February 2000-December 2014 did not reflect "fire sales" as most high-yield funds elected to meet redemptions by reducing their purchases of securities rather than increasing sale of portfolio securities).

[37] Fidelity-FSB 2015 Letter, at 29.

[38] ICI-FSB 2014 Letter, at F-15-F17.

[39] Richardson, *supra* note 22, at 32.

[40] *See* Fidelity-FSB 2015 Letter, at 7-10 (explaining that funds do not and have not failed); Strategic Insight, *supra* note 35, at 3-4 (explaining that large stock and bond funds are more stable due to the heterogeneous nature of mutual

FSOC and FSB have acknowledged that funds and managers close regularly with no systemic impact."[41] Current SEC Commissioner Piwowar also recognized in a recent speech that "there is no evidence that asset managers, investment management funds, and insurance companies pose any threat to the stability of the financial system.[42] In the course of three Consultative Documents, the FSB has failed to identify any instance in which a traditional variable net asset value mutual fund or its manager has ever suffered financial distress or failure having an impact on the global financial system. Rather, the empirical evidence from the past 75 years shows that no manager exits or mutual fund liquidations or closures, which occurred during periods of significant market stress, resulted in a threat to financial stability or caused any systemic market impact.[43]

Thus, we do not believe that the FSB has proven its case concerning systemic risk in the asset management industry, or responded to the overwhelming evidence that such risk does not exist and cannot reasonably be expected to arise. This may be the reason so many terms are undefined and many of the Consultative Document's recommendations are premised on anticipated results from IOSCO's data gathering initiatives, which are yet to be completed. Although, many of the recommendations in the Consultative Document seem sensible in the abstract, there is no nexus between them and the stability of the global financial system. Further, we believe that any new policy recommendations concerning the asset management industry should be made only after IOSCO and its members, like the SEC, collect additional data, conduct an economic analysis (*e.g.*, a cost-benefit analysis) and publish such analysis for public review and comment, as is required of U.S. regulators prior to the introduction of proposed regulations.[44]

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fund investors: "[I]t is our view that large mutual funds and fund management companies . . . are actually more stable than are smaller investment pools with more concentrated investor bases, due to such large entities' diversified ownership by millions of individual investors and their wide and varied marketplace presence.").

[41] *See, e.g.*, Consultative Document, at 8 ("Given that an asset manager's balance sheet is generally very small relative to the size of assets managed, distress at the level of the asset manager should generally pose less of a risk to the financial system than distress across its funds."); Fidelity-FSB 2015 Letter, at 18-19 (arguing mutual fund and managers cannot fail mainly due to leverage restrictions, and noting the Second Consultative Document fails to identify an instance of such failure); First Consultative Document, at 30 ("[F]unds close (and are launched) on a regular basis with negligible or no market impact."); FSOC, Notice Seeking Comment on Asset Management Products and Activities [Docket No. FSOC–2014–0001], Federal Register, Vol. 79, No. 247, December 24, 2014, pp. 77,488-77495 (p. 77,493), *available at* https://www.gpo.gov/fdsys/pkg/FR-2014-12-24/pdf/2014-30255.pdf ("The Council recognizes that asset management firms and investment vehicles have closed without presenting a threat to financial stability. The Council notes that an investment vehicle has a separate legal structure from the asset manager, any parent company, or any affiliated investment vehicles under the same manager. In addition, the assets of the investment vehicle are not legally available to the asset manager, its parent company, or affiliates for the purpose of satisfying their financial obligations or those of affiliated investment vehicles.").

[42] *See* Piwowar, *supra* note 10.

[43] *See* ICI-FSOC 2016 Letter, at B-14 (disputing FSOC hypothesis that mutual fund redemptions contribute to systemic risk by reviewing empirical evidence for stock and bond funds in the past 75 years, which included 2007-2009 financial crisis, the European debt crisis of 2011, the Taper-Tantrum of 2013, the 2015-2016 sell-off in the U.S. high-yield bond market, and the recent U.K. Brexit vote).

[44] *See supra* notes 17-20.

III. "Liquidity Mismatches" Do Not Exist in Most Open-end Funds and Do Not Threaten Global Financial Stability.

The Consultative Document claims that a "key structural vulnerability" from asset management activities is the potential "mismatch" in open-end funds between liquidity of fund investments and daily redemption of fund units.[45] We strongly disagree with the FSB's characterization, which seems to imply that offering daily redemptions means that a fund should only invest in assets that themselves offer daily liquidity. From an economic perspective, there is no material difference between an investor in a fund and an investor that purchases the same assets directly.[46] Each can sell the assets at a market price.

U.S. mutual funds are designed to meet their investors' redemption requests even in a "stressed environment," even though all of their assets may not trade on a daily basis. Existing regulations applicable to U.S. mutual funds require stringent liquidity management practices, including requirements for at least 85% of a fund's portfolio to be in liquid assets and limitations on a fund's holdings of illiquid assets.[47] Recently proposed SEC rules addressing liquidity risk management for U.S. asset managers will impose even stricter requirements on liquidity risk management.[48] Fidelity already employs a number of internal practices to ensure sufficient liquidity in our mutual funds to meet redemption requests, even in stressed markets, as do other mutual fund managers.[49]

Liquidity risk management is inherent in the design and regulation of open-end funds and an important focus for fund managers because redemptions are a normal occurrence for the funds they manage. They are handled, even during historically stressful market conditions, without impacting the global financial system. Rather than contributing to financial instability, mutual funds are actually a natural holder of risky assets from the perspective of minimizing systemic risk.[50] This is the case given that (i) mutual funds employ limited leverage, (ii) any potential losses would be widely dispersed across a fund's full set of shareholders (and would not impact the balance sheet of the asset management firm or other funds managed by the same firm), and

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[45] Consultative Document, at 13.

[46] *See* Richardson, *supra* note 22, at 20 ("in a setting in which assets are fairly priced by funds with floating NAVs, it is not apparent why mutual fund investors are more likely to redeem (*i.e.*, leading to asset sales) than other investors in those assets").

[47] *See* Fidelity-FSB 2015 Letter, at 10, Exhibit 4.

[48] *See supra* notes 12-15.

[49] *See* Fidelity-FSOC 2015 Letter, at 16-17 (listing internal processes used for liquidity management of funds, including portfolio management, cash management, private equity limits, temporary defensive practices, interfund lending, lines of credit, compliance monitoring and oversight, short-term redemption fees, review of dealer investors and fundamental research).

[50] *See* Richardson, *supra* note 22, at 16 ("[g]iven their limited levels of leverage, relatively high degree of transparency, high degree of substitutability, and the pass-through nature of any gains and losses suffered on investments, it seems to me that mutual funds are a natural holder of risk securities in terms of minimizing systemic risk.").

(iii) the transparent nature of fund holdings.[51] Imposing stringent restrictions on investments for all mutual funds is likely to diminish diversification among funds, thereby increasing the potential for herding, volatility during market declines, and amplifying the impact of any financial shocks.[52]

The Consultative Document also fails to recognize that investors in mutual funds understand the differences between the features of mutual funds and bank accounts, which is why they have both types of accounts serving different needs.[53] Mutual fund investors are overwhelmingly long-term investors. Investors in non-money market mutual funds are almost exclusively individuals, almost all of whom (91 percent) are investing for retirement.[54] Indeed, over half of the household assets invested in mutual funds are invested through retirement accounts, such as IRAs and 401(k)s.[55] The long-term investment perspective of investors in mutual funds is borne out by the low redemption rates of these investors seen during recent market downturns.[56] Therefore it is unreasonable for the FSB to assume, by alleging liquidity "mismatches" in open-end funds, that mutual fund investors have the same low risk tolerance and need for liquidity in their mutual fund investments as they do in their bank accounts.

IV. Additional Tools May Be Useful; But Existing Tools Available to U.S. Fund Managers Are Sufficient to Manage Redemption Activity During Stressed Conditions, Should the Need Arise.

Although additional tools may be useful in some jurisdictions, liquidity and redemptions are already well managed in U.S. mutual funds by their managers as discussed above. Therefore, we do not see a need for the FSB's recommendation that authorities widen the availability of liquidity risk management tools made available to mutual funds in order to increase the likelihood that redemptions are met under stressed conditions.[57] The inability of a mutual fund to meet investor redemptions is an extremely rare event. The Investment Company Institute ("ICI") was only able identify six instances within the past 75 years in which the SEC allowed a long-term mutual fund to suspend investor redemptions.[58] The ICI analyzed one high-yield bond fund in particular that suspended redemptions in 2015 and found that even where all of the elements of "investor-driven contagion" that regulators such as the FSB have hypothesized were

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[51] *See* ICI-FSOC 2015 Letter, at 11 ("the transaction costs of constructing and maintaining a properly diversified portfolio of directly held investments would be prohibitively expensive for most retail investors, and would have an adverse effect on investment returns.").

[52] *See* ICI-FSOC 2015 Letter, at 6.

[53] *See* Fidelity-FSB 2015 Letter, at 24 (the largest mutual funds (reflecting more than $100 billion in AUM) accounted for less than 1 percent ($2.14 trillion) of global financial assets as of 2013, in contrast to banks designated as G-SIBs which accounted for over $45 trillion, or 15 percent, of global assets).

[54] *See* Investment Company Institute, 2016 Investment Company Fact Book, at 111, figure 6.2 (hereinafter, "ICI Fact Book"), *available at* http://www.icifactbook.org .

[55] *Id.*

[56] *See* ICI-FSB 2014 Letter, at F-6-F-7.

[57] Consultative Document, at 20.

[58] ICI-FSOC 2016 Letter, at 9, fn. 26.

present, there was minimal impact to the high-yield bond fund markets or the financial markets generally.[59]

We do not believe that post-event measures such as redemption gates or suspensions are an effective measure for managing liquidity and redemptions in most open-end funds. Redemption gates applied beyond money-market funds can serve to create problems that would not exist without them, depending on the method by which the gates are imposed, and may in fact incentivize investors to exit a fund before a redemption gate is lowered.[60] This is why we believe is it especially important for the FSB and IOSCO, in determining whether residual risks exist and warrant specific policy responses, to consider the full array of mitigants to redemption risk. Tools that may be used to manage redemption activity include excessive trading restrictions and redemption fees that allow funds to recoup costs incurred as a result of short-term trading, and also promote a more stable, long-term investment perspective among fund shareholders. In addition, defined contribution plans and plan sponsors can limit trading opportunities for plan participants. Many funds impose transaction fees including purchase fees and exchange/transfer fees that also can impact an investor's decision to redeem. Since the majority of mutual fund investors are saving for retirement,[61] there are also economic incentives for investors to keep assets in retirement accounts to allow those assets to grow tax free and avoid early tax withdrawal penalties. In our opinion these economic incentives, investment trends and tools, which are utilized in the normal course and not only during stressed conditions, are sufficient mitigants to any concerns that investors may make sudden and excessive redemption requests.

V. A Small Subset of Funds Where Liquidity Risk May Be Elevated Should Not Form the Basis for Recommendations for the Entire Asset Management Industry.

We agree with the FSB's recognition of the resiliency of open-end funds. The FSB is correct that, with the exception of some money market funds, they "have not created financial stability concerns in recent periods of stress and heightened volatility."[62] On the contrary, the long-term equity capital base they provide has been a stabilizing influence. This is a fact repeatedly advanced by Fidelity and other commentators, and is supported by substantial historical evidence.[63] The FSB, in its First Consultative Document, also acknowledged this to be true with respect to mutual funds in particular.[64]

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[59] ICI-FSOC 2016 Letter, at B-6, B-7.

[60] *See* Fidelity-FSOC 2015 Letter, at 12, 21.

[61] *See* ICI Fact Book, at 120 ("91 percent of mutual fund-owning households indicated that saving for retirement was one of their financial goals, and 72 percent said it was their primary financial goal."); *see also id.* at 12 (showing that at year-end 2015, mutual funds managed 54% of the assets held in retirement accounts).

[62] Consultative Document, at 1.

[63] *See e.g.*, Fidelity-FSOC 2015 Letter, at 7 (citing an ICI study of equity fund flow data from 1955 through 2013 showing that in the worst financial crisis (from November 2007 to March 2009), net outflows from equity funds was only 4.1%. ICI data also reflected that mutual fund investors traded far less during the 2008-2009 financial crisis than did other investors, discounting any allegations concerning "runs" which could infect the financial markets); ICI-FSB 2014 Letter, at F-6, F-7; Strategic Insight, *supra* note 35 (using a slightly different set of data, finding

In recognition of the lack of contrary evidence linking mutual fund flows to systemic risk historically, the FSB is turning its focus towards liquidity and redemption risk in fixed income mutual funds. The Consultative Document suggests that "the increasing holdings of fixed income assets by investment funds suggest that risks may have increased in recent years."[65] As discussed below, statistical evidence shows that fixed income funds constitute only a small portion of the asset management industry and redemptions at these funds have been modest at best during stressed periods. Further, these funds hold a small percentage of the U.S. bond market. Although their assets under management have increased they have been consistent with increases in the sizes of bond markets. Therefore any potential risk associated with these funds cannot be considered "systemic." Alternatively, even if the FSB's premise that fixed income funds pose systemic risk is correct, the FSB should address only issues concerning those products and not make policy recommendations that apply to all open-end funds.

To make its case, the FSB cites the over $76 trillion in global assets under management, 40% of which ($37 trillion) is invested in regulated open-end mutual funds.[66] Excluding ETFs and institutional funds, $31 trillion is invested in open-end mutual funds and $8 trillion of that is in fixed income mutual funds. Fixed income mutual funds' holdings constitute only 10% of the entire U.S. bond market, meaning that 90% of bonds are held outside of mutual funds and therefore outside of the FSB's focus in the Consultative Document.[67] The FSB also concedes that the rate of growth of assets under management for fixed income mutual funds "does not appear to be expanding faster than the pace at which the bond markets are expanding."[68] For this reason, it is unclear to us how this "growth" in fixed income assets held in mutual funds could be considered material, much less be considered a source of global systemic risk. Nor does the FSB point to any other factors that demonstrate how this "growth" has led to "structural vulnerabilities" that have never manifested before, but should concern us now.

A. Redemption Activity in High-Yield Bond Funds During Stressed Market Conditions Has Historically Not Been Material.

As is the case with equity fund flows, redemptions at high-yield bond funds (which are considered less liquid than other types of fixed income mutual funds), during historically stressed

monthly inflow and outflow rates for equity and balanced funds typically fluctuate in a narrow range, around 2-3 percent of assets, with very few spikes over 4 percent).

[64] First Consultative Document, at 30, n. 38 ("[E]ven when viewed in the aggregate, no mutual fund liquidations led to a systemic market impact throughout the [2000-2012] 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.").

[65] Consultative Document, at 10.

[66] *Id.* at 4.

[67] *See* Investment Company Institute, Models vs. the Real World-Why Bond Funds Aren't the Bond Market, Chris Plantier and Sean Collins (February 25, 2016), *available at* https://www.ici.org/viewpoints/view_16_nyfed_bond_flows_02.

[68] Consultative Document, at 5.

periods have been modest. An ICI study that reviewed activity in high-yield bond funds during the recent financial crisis found that redemptions in these types of funds did not have a negative material impact on the financial markets.[69] The ICI looked at the "contingencies" that are assumed to occur in order for mutual fund redemptions to impact financial stability during stressed markets, including that: (1) mutual fund investors will "run" to redeem large amounts of shares from declining mutual funds, (2) mutual funds will sell their most liquid assets first to meet redemptions, and (3) large sales by mutual funds to meet redemptions will result in a "spillover effect" causing negative impact to the financial markets as a whole.[70] The ICI's results, which were based on actual experiences in the high-yield bond market from 2014 to 2016 – a period of extensive volatility in that market and others – proved the opposite to be true with respect to the behavior of these fund investors, fund managers and other market participants.

The ICI study showed that redemptions in high-yield mutual funds during this time period were only "modest" and that fund managers and other investors were not only selling, but also *purchasing* shares in high yield bond funds during this period.[71] The net result was that trading volumes of high yield bonds actually *rose* during December 2015.[72] This is consistent with another study cited by the ICI showing that during the decline of the securitized mortgage market in 2007, mutual funds were aggregate net *buyers* rather than net sellers of corporate bonds, further disputing the "contagion" theory to support systemic risk policies for mutual funds and their managers.[73] This is consistent with the stabilizing effect of mutual funds due to investor behavior[74] and effective portfolio management strategies.[75]

[69] ICI-FSOC 2016 Letter, at 5.

[70] Notably, these are the same "contingencies" cited by the FSB in assuming investment funds contribute to structural vulnerabilities. *See supra* note 8.

[71] ICI-FSOC 2016 Letter, at 6, A-3 (citing a third-party 2007 stating "[f]unds experiencing extreme inflows or outflows do not appear to transact with any greater frequency in larger, more liquid, or better-performing holdings than funds that are subject to moderate flows. This suggests that funds experiencing extreme inflows or outflows do not mitigate the costs of their liquidity demands by transacting selectively in holdings.").

[72] *Id*. at 9; *see also id.* at A-3 (citing a third-party paper that suggests returns of minus 5 percent on corporate bond funds might lead to an expected aggregate outflow of only 1 percent of their assets).

[73] *Id.* at A-5.

[74] *See* ICI-FSOC 2015 Letter, at 20 (mutual fund investors' automatic payroll contributions to 401(k) plans or other defined contribution plans, investing strategies of dollar-cost averaging, dividend reinvestment and portfolio rebalancing all have countercyclical stabilizing effects on market volatility).

[75] *Id.* at 28 ("Portfolio management of stock, bond, hybrid and other funds can provide natural stabilizers for their respective markets, with these funds buying some undervalued securities during a downturn and selling some overvalued securities in a bull market."); *see also infra*, note 115 (discussing automatic rebalancing of hybrid funds which results in equity purchases when stock prices decline, and reduction of equity holdings when stock prices increase).

B. The "Spillover Effect" From Redemptions in High-Yield Mutual Funds During Stressed Market Conditions Is Speculative and, Even if True, Is Not Systemically Significant.

While the FSB references a New York Federal Reserve Bank (the "New York Fed") study[76] for evidence that holdings of corporate bonds have increased, the Consultative Document ignores a subsequent New York Fed study[77] that confirms potential spillover from extreme redemptions at high-yield bond funds[78] is minimal. The authors of the second study analyzed the potential for spillover effects from a "fire sale" based on extreme assumptions of redemptions at funds deemed similar to the Third Avenue Focused Credit Fund, a high yield bond fund that suspended investor redemptions in December 2015. The New York Fed study was based on an assumption that over 50 percent of these funds' assets[79] would be redeemed almost simultaneously by investors – over ten times as large as the greatest monthly redemptions seen during recent periods of market stress, including the recent global financial crisis.[80]

Even using this extreme assumption of massive redemptions across high-yield bond funds, the New York Fed study found that the potential spillover losses in assets for *all* U.S. open-end mutual funds totaled at most $9 billion.[81] While $9 billion is not an insignificant figure, in the context of the total taxable bond mutual funds (non-government) and hybrid mutual fund market (which hold a mix of stock and bonds), which totaled $3.89 trillion in December

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[76] Consultative Document, at 5, fn. 16

[77] Nicola Cetorelli, Fernando Duarte, Thomas Eisenbach, and Emily Eisner, Quantifying Potential Spillovers from Runs on High-Yield Funds (Feb. 19, 2016) (hereinafter, "New York Fed Study"), *available at* http://libertystreeteconomics.newyorkfed.org/2016/02/quantifying-potential-spillovers-from-runs-on-high-yield-funds.html#.V4eqWP7rvct ("To sum up, our analysis shows that high-yield mutual funds, which share some common features with Third Avenue FCF, hold approximately $280 billion in assets. If these funds experienced a run, forcing each fund to liquidate half its assets, we estimate that the associated fire-sale spillover losses in the entire universe of mutual funds would be about $9 billion. These fire-sale spillovers amount to six to seven cents for each dollar of shocked TNA. These numbers seem relatively small and nonsystemic, although they reflect the specific set of assumptions illustrated above."); *see also* ICI-FSOC 2016 Letter, at 10 ("the New York Federal Reserve's own research suggests that even extremely large outflows from bond funds—assumed outflows far greater than any ever seen in history—simply don't pose systemic risks. The Fed economists themselves seem to agree, noting that 'in this set of funds, no particular fund seems capable—by virtue of its size or asset holdings—to impose significant large fire-sale spillovers on its own.' We think that their research actually points to a stronger conclusion: outflows from all bond funds in aggregate don't seem capable of imposing the kinds of hypothetical fire-sale and spillover risks that the New York Fed's research discusses.").

[78] The New York Fed study specifically focused on the holdings of a sample of funds consisting of high-yield, corporate bond, and multisector funds. These are cumulatively referred to as "high-yield bonds" for discussion purposes.

[79] The New York Fed study calculated total assets in high-yield bond funds as $280 billion, thus 50 percent redemption rate assumed that over $140 billion in assets would be redeemed by investors almost at once.

[80] ICI-FSOC 2016 Letter, at 10.

[81] Chris Plantier and Sean Collins, Investment Company Institute Viewpoints, New Research by New York Fed Confirms: Bond Funds Don't Pose Systemic Risks (February 23, 2016), *available at* https://www.ici.org/viewpoints/view_16_nyfed_bond_flows (even during December 2015, the same month that Third Avenue Capital's Focused Credit Fund suspended redemptions, outflows from the median individual high-yield fund were just 2.4 percent of its assets. And no high-yield fund had outflows of 50 percent of its assets).

2015, the "spillover effect" amounts to only 23 basis points (0.23 percent) of these funds' total assets.[82] Including the assets of all long-term taxable mutual funds in the calculation (which totaled $12.304 trillion in December 2015), the "spillover effect" becomes even less significant – amounting to just 7 basis points (0.07 percent) of those funds' assets.[83] Thus the New York Fed study empirically shows that even using aggressive assumptions about investor redemptions that are far more extreme than historical experience, any potential "spillover effect" to the financial markets is "relatively small and nonsystemic."[84]

VI. Operational Risk Does Not Equate to Systemic Risk and Although We Recognize the Importance of Business Continuity Planning for Asset Managers, We Do not Believe There is a Need for Separate Transition Plans.

The Consultative Document claims that operational risk in transferring investment mandates during stressed market conditions is also a potential source of systemic risk.[85] As with many of the Consultative Document's suppositions, this alleged risk is based on hypothetical scenarios[86] that have never materialized,[87] and incorrectly conflates size with increased risk to global financial stability.[88] As the FSB, FSOC and the SEC acknowledge, asset managers routinely exit and enter the market and transfer client accounts without any impact to global financial stability.[89] There is also no correlation between an asset manager's own size or the amount of assets it manages and increased operational risk resulting in globally systemic implications. We recognize the importance of comprehensive business continuity policies that address operational risk, and we support those types of proposals advanced by regulators, such as the recently proposed rulemaking by the SEC.[90] However, we do not believe there is a need for

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[82] *See* Chris Plantier and Sean Collins, Investment Company Institute Viewpoints, *supra* note 81.

[83] *Id.*

[84] *See* New York Fed Study, *supra* note 77.

[85] Consultative Document, at 28.

[86] *Id.* (noting operational difficulties "*could* potentially" become a financial stability concern "*if*" they materialized during "stressed market conditions" and "*if*" difficulties are serious enough for investor they "may" lose confidence in the funds).

[87] *Id*. (FSB conceding "these challenges have been infrequent in the past and have not raised financial stability issues"); *id.* at 30 ("Historically, there have not been serious operational incidents during stressed conditions. Thus it is difficult to assess the potential materiality of such operational difficulties.").

[88] *Id.* at 28 (noting particular risks from asset managers "of sufficient scale or complexity" and that redemptions "at a large manager" can potentially affect market prices particularly during stressed conditions); *id.* at 31 (recommending requirements or guidance for asset managers that are "large, complex and/or provide critical services").

[89] *See supra* note 27; *see also* Adviser Business Continuity and Transition Plans, 81 Fed. Reg. 43530, at 43535 (July 5, 2016) (hereinafter, "SEC Business Continuity and Transition Plan Proposal"), *available at* https://www.gpo.gov/fdsys/pkg/FR-2016-07-05/pdf/2016-15675.pdf ("In the normal course of business, it is our understanding that advisers routinely transition client accounts without a significant impact to themselves, their clients, or the financial markets").

[90] *See* Letter from Marc. R. Bryant, Senior Vice President & Chief Legal Officer, Fidelity Mgmt. & Res. Co. to Brent J. Fields, Secretary of the U.S. Securities and Exchange Commission (Sept. 6, 2016) (hereinafter "Fidelity-SEC 2016 Letter"), *available at* https://www.sec.gov/comments/s7-13-16/s71316-17.pdf.

separate transition plans for asset managers since there is no proven nexus between operational risk at an asset manager and global financial stability.

Mitigation of operational risks that may occur in transferring accounts, assets and investment mandates (in both stressed and ordinary market conditions) can be entirely addressed through appropriate business continuity planning and the existing asset management regulatory framework, which enables these transitions to occur daily, in high volumes, regardless of financial distress. This view is consistent with the FSB's observation in its recent guidance on operational continuity for banking firms in resolution that in "most cases, going concern operational continuity is considered in the context of a firm's resilience and business continuity planning."[91] Even in the banking context – where the rapid dissolution of banks has been shown to impact financial stability – regulators view operational risks as within the confines of business continuity planning. This further proves a lack of necessity for separate operational transition planning in the asset management context, where failures are rare and have not impacted financial stability or required special resolution plans.

With respect to business continuity planning for U.S. registered investment asset managers, we direct the FSB to the SEC's recent rulemaking proposal requiring written business continuity and transition plans that are reasonably designed to address operational risks related to a significant disruption in an asset manager's business.[92] The SEC's business continuity proposal codifies and supplements existing practices adopted by U.S. registered investment advisers, including Fidelity, pursuant to Rule 206(4)-7 under the Investment Advisers Act of 1940 and Rule 38a-1, which required advisers to adopt written compliance policies and procedures addressing operational risk exposure for the adviser and its clients, including business continuity plans.[93] Notably, the SEC's proposal is applicable to all SEC registered asset managers, regardless of size, observing that *all* advisers face operational risks, not only "large" or "complex" managers. We therefore request that the FSB defer any further initiatives concerning business continuity or resolution planning policies for U.S. funds and fund managers to the SEC, where efforts to enhance existing business continuity requirements are already underway.

As Fidelity noted in the Fidelity-SEC 2016 Letter, we fully support the SEC's goal of ensuring that all asset managers have business continuity plans that mitigate the effects of any material disruption on clients and believe that business continuity planning is required to meet an adviser's fiduciary duty to mitigate, and reduce the likelihood of, disruptions to an asset manager's business that may negatively affect its customers.[94] As we noted in the Fidelity-SEC 2016 Letter, we believe that robust business continuity planning protects against operational

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[91] Fin. Stability Bd., Guiding on Arrangements to Support Operational Continuity in Resolution, at 8 (Aug. 18, 2016), *available at* http://www.fsb.org/wp-content/uploads/Guidance-on-Arrangements-to-Support-Operational-Continuity-in-Resolution1.pdf.

[92] *See* SEC Business Continuity and Transition Plan Proposal, *supra* note 89.

[93] *See* Final Rule: Compliance Programs of Investment Companies and Investment Advisers, SEC Release Nos. IA-2204, IC-26299 (Dec. 17, 2003), *available at* http://www.sec.gov/rules/final/ia-2204.htm.

[94] *See* Fidelity-SEC 2016 Letter, at 1-2.

risks that clients may face due to distress in the financial markets or distress at an asset manager or its fund, and therefore, separate transition plans that account for operational risks during an asset manager's exit from the industry are unnecessary.[95] We also reiterated our view that there is no need for resolution planning requirements that address operational risks for investment managers, whether structured as "living wills" [96] or a version thereof, because the probability and impact of a sudden failure are both extremely low.[97] Unlike banks or insurance companies, investment managers are not prone to "failure" or sudden financial distress because they operate in an agency-only capacity, use little or no leverage, do not rely on government support, and do not use their balance sheets when trading client assets. These restrictions limit the potential for "financial distress" at asset managers or systemic market impact due to the expectation of bailouts, as was the case with the banking industry during the 2008 financial crisis. When a typical fund liquidates, the resulting impact to customers is little different than if the customers had invested directly in assets sold by the fund. This is in sharp contrast with the banking industry during the 2008 financial crisis, which due to the use of leverage, proprietary trading, and off-balance sheet transactions, lacked sufficient capital to meet their obligations, and required stabilization through government bailouts.

Unlike banks, which rely on access to credit and liquidity in order to function, there is no clear nexus between financial stress and operational difficulties in asset management. A typical investment manager does not rely on the financial markets to fund its operations, in contrast to banks which rely on third-party financing and can face capital shortfalls in the event of distress. A recent FSB publication that confirmed the need for temporary funding for banks in resolution also reflects why the same requirement is unnecessary for asset managers:

> Work to date (e.g. in the first round of the FSB Resolvability Assessment Process (RAP)) has found that funding poses a material impediment to the resolution of global systemically important banks (G-SIBs). In particular, there is a risk of insufficient liquidity to maintain critical operations arising from the G-SIB's inability to roll over short-term borrowing or loss of access to alternative sources of credit. This work also found that more analysis and understanding of funding

[95] *See* Fidelity-SEC 2016 Letter, at 4-13.

[96] *See* Dodd-Frank Act §165(d), *available at* https://www.fdic.gov/regulations/reform/dfa_selections.html#1 (requiring nonbank financial companies designated under the Act to provide "the plan of such company for rapid and orderly resolution in the event of material financial distress or failure" and that such plan shall include "(a) information regarding the manner and extent to which any insured depository institution affiliated with the company is adequately protected from risks arising from the activities of any nonbank subsidiaries of the company; (b) full descriptions of the ownership structure, assets, liabilities, and contractual obligations of the company; (c) identification of the cross-guarantees tied to different securities, identification of major counterparties, and a process for determining to whom the collateral of the company is pledged; and (d) any other information that [may] jointly require by rule or order.").

[97] *See* Fidelity-FSOC 2015 Letter, at 38 ("The probability that either funds or their managers would suddenly become insolvent and file for bankruptcy protection is extremely low and easily dismissed as a potential threat to financial stability. Empirically, fund mergers and liquidations have happened regularly, even in times of market stress, and there is no evidence that they have had a systemic impact on the market in the past. Given their attributes described above and the fact that they do not provide a critical function or service without ready substitutes, there is no sound theory as to why they might in the future.").

> and liquidity needs in resolution is necessary, in particular liquidity and funding needs in different currencies.[98]

There is no similar funding need for asset managers or their back office operations, which helps explain why they exit the market regularly and transition clients and investment mandates without any special resolution mechanism or plan and without impacting financial stability.

The focus on funding and financial stress is inapposite to asset managers. An investment manager can face operational difficulties with or without a stressed market. Conversely, an investment manager will not necessarily have operational issues during a stressed market. In fact, there may be little effect beyond an increase or decrease in volume. Most operational challenges arise from geopolitical events such as wars and terrorist attacks, natural disasters such as blizzards, hurricanes and tsunamis, problems at service providers or counterparties, and system outages due to execution failures, software problems and power outages, which are independent of an asset manager's financial condition. This explains why, as the FSB admits, "[h]istorically, there have not been serious operational incidents during stressed conditions. Thus, it is difficult to assess the potential materiality of such operational difficulties."[99]

In the normal course and in all market conditions, investment managers transfer large volumes of client assets and accounts without significant impact to clients, themselves or the financial markets.[100] This is true even during non-routine disruptions at large investment managers that resulted in transitions to new advisers or new ownership.[101] This is largely because investment funds and their managers are highly substitutable, enabling investors with numerous alternative choices to transition accounts easily on a daily basis, leaving global financial stability unaffected.[102]

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[98] Fin. Stability Bd., Guiding Principles on the Temporary Funding Needed to Support the Orderly Resolution of a Global Systemically Important Bank (G-SIB) (Aug. 18, 2016), *available at* http://www.fsb.org/wp-content/uploads/Guiding-principles-on-the-temporary-funding-needed-to-support-the-orderly-resolution-of-a-global-systemically-important-bank-%E2%80%9CG-SIB%E2%80%9D.pdf.

[99] Consultative Document, at 30.

[100] *See id.* at 41-42 (noting routine nature of mergers and liquidations of funds and that from 2003 through 2013, over 6,100 mutual funds were merged or liquidated). *See also* First Consultative Document, at 30, fn. 38 (conceding that thousands of mutual funds liquidated from 2002-2012 with no discernible impact on financial stability).

[101] *See* Consultative Document, at 42 (citing successful spinout of Neuberger Berman from Lehman Brothers during financial crisis).

[102] *See* Fidelity-FSB 2015 Letter, at 31 ("Mutual funds remain 'highly substitutable.' For any market segment popular enough to attract a material amount of investment, there will be dozens if not hundreds of investment fund choices. After all, there are over 16,000 registered investment companies, including almost 9,000 mutual funds, in the United States alone. As a result, all of the biggest mutual funds have hundreds of direct competitors offering similar investment strategies and, over time, the identities of the biggest funds change (five of 2004's top 20 largest funds did not make the list in 2014). History confirms that when individual mutual funds perform poorly or fall out of favor with investors for other reasons, global financial stability is completely unaffected."); *see also supra* note 27 (citing FSB prior Consultative Documents and FSOC notices all acknowledging that asset managers exit the industry and clients replace managers without significant impact to themselves or the financial markets).

A further safeguard for U.S. mutual fund customers is that their assets are required to be held at third-party qualified custodians and segregated from the asset manager's assets. As a result, transitioning funds or customer accounts from one manager to another is a streamlined process that in many cases may not involve the physical movement or sale of assets. Since asset managers are generally highly substitutable, in the ordinary course, customers routinely move assets out of funds and accounts, and terminate advisory relationships, without any impact to themselves or the financial markets.[103]

Asset management is also a valuable service, but not critical. Multiple studies have found that the majority of global financial assets are self-managed, not managed by third-party managers.[104] Asset owners can manage their assets alone, outsource management to an adviser, or do both. If an advisor were to discontinue managing a particular fund due to a change in strategy or closure of a fund, a customer has many choices. The customer can self-manage, continue the same strategy by moving their assets to another fund offered by the same adviser, or transfer their assets to another adviser offering the same strategy. There is no shortage of advisers or funds for customers to choose from as competition to attract assets from customers ensures a constant offering of mutual fund and other investment products. Since 2013, the overall number of U.S. registered investment companies, which includes almost 9,500 mutual funds, has remained steady at approximately 16,000 funds, despite changes in the types and identities of the individual funds.[105] Fund sponsors routinely enter and exit the market in response to investor demand. They also create new mutual funds to meet this demand and close mutual funds that are not successful. The ICI reports that from year-end 2009 to year-end 2015, the number of mutual fund sponsors increased from 682 to 873, with 440 sponsors entering the market and 249 sponsors leaving.[106] The ICI reports that in 2015 there were $15.7 trillion in U.S. mutual fund assets under management and that in 2015 mutual funds had a net cash outflow of $102 billion in 2015, in contrast with a net cash inflow of $104 billion in 2014.[107] In 2015, customers redeemed $123 billion, on net, from long-term funds, and added $21 billion, on net, to money market funds.[108] Even though ETF assets have increased significantly as they have

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[103] *See* SEC Business Continuity and Transition Plan Proposal, at 43535 ("Pooled investment vehicle clients generally have the ability to terminate the advisory contract of the adviser or remove the governing body that may provide advisory services (*e.g.,* general partner or managing member) and appoint a new adviser or governing body if they so desire, while separate account clients can generally terminate the advisory contract and appoint a new adviser to manage their assets, all while their assets are typically maintained at a qualified custodian.").

[104] McKinsey & Company estimates that more than three quarters of financial assets are either unmanaged or managed internally by asset owners. McKinsey & Company, Strong Performance but Health Still Fragile: Global Asset Management in 2013: Will the Goose Keep Laying Golden Eggs? at 8, Exhibit 2 (July 2013), *available at* http://www.asset-management-summit-2015.com/pdf/2013_Asset_management_brochure_20130723.pdf (showing that the asset management industry managed a market share of 23.9 percent of total global financial assets in 2012); *see also* ICI Fact Book, at 11 (as of year-end 2015, mutual funds managed only 22 percent of U.S. household financial assets).

[105] *See* ICI Fact Book, at 22.

[106] *Id.* at 16.

[107] *Id*. at 9.

[108] *Id.* at 10.

gained popularity with investors, over 100 ETFs are on pace to close in 2016 in the U.S., with 41 ETF closings in August alone. [109]

Overall, we believe that the FSB underestimates the volume of customer assets and accounts that are in motion daily and underestimates the robustness of the asset management functions that are well versed in transferring customer assets. They also overestimate the relevance of financial stress to fund operations. As with many of the FSB's other recommendations, their concern about operational risks faced by asset managers in transferring client accounts is unrelated to global financial stability and we direct the FSB to provide empirical evidence supporting its conclusion prior to advancing any additional rulemaking on this topic.

VII. The Consultative Document Fails to Consider Whether the Benefits of Collective Funds and Professional Management Would Be Reduced by the Policy Recommendations.

Collective investment funds and professional third-party management create significant economic and financial stability benefits that are widely acknowledged. The economic benefits accrue to individual retail investors,[110] issuers like businesses and governments,[111] and to everyone via investment in economic growth.[112] Collective investment and professional management similarly enhances financial stability in many ways, including diversifying sources of funding,[113] distributing risk broadly rather than concentrating it, financing assets primarily

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[109] *See* The Great August Fund Die-Off, MarketsMedia (Sept. 6, 2016), available at http://marketsmedia.com/great-august-fund-die-off/.

[110] For example, 95% of mutual fund investors are retail. *See* ICI Fact Book, at 29. Benefits to retail investors include: access to diverse investments for middle income investors, cost effective savings for retirement and other lifetime goals, risk mitigation, professional management and consistency of regulations. *See id.* at 120-26; *see also* Richardson, *supra* note 22, at 41; ICI-FSOC 2015 Letter, at 11 ("Individuals hold 95 percent of stock and bond mutual fund assets, typically to save for goals such as college and retirement. They overwhelmingly choose mutual funds as a cost effective way to achieve their objectives, through a shared interest in a professionally managed pool of securities that is protected by comprehensive regulation under the federal securities laws. The vast majority of these investors would be unable to replicate such investment exposure by directly holding securities themselves.").

[111] Benefits to issuers include low cost funding, diversification of funding sources beyond banks. *See* Int'l Monetary Fund, Risk Taking, Liquidity, and Shadow Banking: Curbing Excess While Promoting Growth, Global Financial Stability Report, 33 (Oct. 2014), *available at* http://www.imf.org/external/pubs/ft/gfsr/2014/02/pdf/text.pdf ("from a financial stability perspective, credit intermediation through asset managers and markets has advantages over that through banks."); Richardson, *supra* note 22, at 40-41 (arguing the imposition of the Volcker Rule within the Dodd-Frank Act "is to move risk-taking activities away from the systemically important risky banking sector to the less levered, capital market sector.").

[112] *See* Piwowar, *supra* note 10 ("Capital markets channel savings from individual investors to investments in the real economy, providing a significant source of financing for the corporate sector. These investments have always been about risk and investors in the capital markets operate with the knowledge that the capital they invest is subject to risks and, unlike bank deposits, it is not guaranteed. Investors knowingly make this tradeoff between the risk of loss of principal and the hope of earning a higher return on their investment. It is this risk taking that has enabled capital markets to be a key driver of economic growth.").

[113] *See e.g.*, Jonathan Hill, Member, European Comm', Speech at the Finance Watch Conference: Finance at your Service – Capital Markets Union as an Instrument of Sustainable Growth (Feb. 4, 2015), *available at*

with equity rather than debt, providing financing without relying on government support or creating the associated moral hazard, and providing stable long-term funding.[114] By holding diverse assets and pursuing diverse strategies with various business models, mutual funds and other market participants provide benefits to investors, the capital markets and the real economy by ensuring more heterogeneous, competitive, efficient and resilient capital markets.[115] It is a key attribute that makes funds and capital market financing inherently more flexible and resilient than banking.

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http://europa.eu/rapid/press-release_SPEECH-15-4144_en.htm ("Well-functioning capital markets also help encourage greater diversity in funding, which reduces concentration of risk so they not only free up capital for growth but also support and strengthen financial stability. After all, it's important to remember that 'capital markets' are not some abstract construct – they are someone's pension savings, someone's 'rainy day' money which is channelled to growth."); Int'l Monetary Fund, *supra note* 111, at 31 ("The nonbank sector, particularly mutual funds and ETFs, has become an increasingly important supplier of credit, as many banks continue to have limited balance sheet space to support private sector credit.").

[114] Evidence of these benefits have been cited by Fidelity in past comment letters (See Fidelity-FSOC 2015 Letter, at 7) and acknowledged by the FSB, EU Commissions and other officials. *See, e.g.*, First Consultative Document, at 29 ("[F]rom a purely systemic perspective, funds contain a specific 'shock absorber' feature that differentiates them from banks."); *see also* Nellie Liang, Dir., Program Direction Sec. of the Off. of Fin. Stability Pol'y & Res., Bd. Of Governors of the Fed. Res. Sys., Remarks at the Brookings Institution Asset Management, Financial Stability and Economic Growth Conference (Jan. 9, 2015), *available at* https://www.brookings.edu/wp-content/uploads/2014/12/20150109_asset_management_transcript.pdf ("Mutual funds in their current form have been around for a long time . . . without noticeably contributing to systemic risk."); Sir Jon Cunliffe, Deputy Governor Fin. Stability, Bank of Eng., Speech at the City of London Corporation and Open Europe Conference: Financial Stability, the Single Market and Capital Markets Union, 7 (Jan. 20, 2015), *available at* http://www.bankofengland.co.uk/publications/Documents/speeches/2015/speech789.pdf ("It is very probable that one of the reasons the US has recovered faster from its financial crisis than Europe is that in the US banks do not dominate the provision of finance to anything like the same degree as in the EU.").

[115] Nicholas Beale et al., Individual Versus Systemic Risk and the Regulator's Dilemma, 108 PNAS 12,647 (Aug. 2, 2011), *available at* http://www.pnas.org/content/108/31/12647. Recent investment trends show a movement towards investors holding more diversified funds such as balanced funds, fund-of-funds and hybrid funds, which themselves provide additional stabilization to global financial markets. *See e.g.*, John Rogers, President & CEO, CFA Inst. & Member, Systemic Risk Council, Remarks at the Financial Stability Oversight Council Conference on Asset Management in Washington D.C., 203 (May 19, 2014), *cited in* Letter from Timothy W. Cameron, Head & Managing Director, SIFMA Asset Management Group, and John Gidman, President, Ass'n of Institutional Investors to U.S. Dep't of Treasury (Sept. 23, 2014), *available at* http://www.sifma.org/issues/item.aspx?id=8589951018 (describing how rebalancing by "institutional investors and retirement savings plans" has a countercyclical effect since "increasing amounts of assets managed by the largest U.S. managers are defined contribution, defined benefit, endowment [and] foundation assets. . . . Now, these investors tend to rebalance in a disciplined way, so . . . when the equity market goes down relative to other asset classes, they will rebalance by buying more equities and vice versa. And . . . so-called hybrid, and also target date funds . . . [which] are becoming the default option for most U.S. defined contribution plans, . . . will automatically rebalance based on their prospectus. So, in other words, you have increasing amounts of assets, which lean against the direction of market trends. When stocks go down, they rebalance back into stocks. When stocks go up, they rebalance by shaving down on the equity holdings. . . . And so I would argue that there is at least as strong a counter-cyclical force that exists inherently in the U.S. asset management industry."); ICI-FSOC 2015 Letter, at 28 ("Portfolio management of stock, bond, hybrid and other funds can provide natural stabilizers for their respective markets, with these funds buying some undervalued securities during a downturn and selling some overvalued securities in a bull market. For many kinds of funds, the investment objectives, policies, and strategies described in the funds' prospectuses may dictate this outcome. Hybrid funds, target risk funds and target date funds all may need to sell securities that have increased in value and buy securities that have fallen in value in order to keep their portfolios in balance.").

The Consultative Document fails to consider whether the benefits of collective funds and professional management would be reduced or altered by its policy recommendations.[116] A recent white paper issued by a coalition representing U.S. corporations Amazon, Apple, Google, Intuit and PayPal warned that addition financial services regulations can chill innovation, investment or slow time to market, ultimately harming consumers and businesses that benefit from easier access, more competition and more affordable services.[117] As the SEC's Commission Piwowar also recently cautioned, "[t]rying to mitigate risks related to the asset management industry on a macro level likely would result in a narrowing of the differences in the way assets are managed, which could result in all financial firms having similar investments. . . Add this to the risk posed by already highly correlated bank balance sheets and you have a recipe for the collapse of the entire financial system."[118] Any new policy recommendations regarding the regulation of asset management products or activities should be supported by an analysis of their impact on these benefits that demonstrates that there is a need for new policies and they will do more good than harm.

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We appreciate the opportunity to comment on the Consultative Document. The deliberative empirical approach that we recommend implicitly recognizes that every risk is not worth addressing if its probability or impact is low or if the benefits of the solution are likely to be outweighed by its costs. In the context of hypothetical global systemic risks, this threshold is even higher since any policy is intended to impact the global financial system and the risk it addresses needs to be both reasonably likely and material to global financial stability in order for it to warrant remediation. We question whether after three Consultative Documents, spanning two years and nine months, with additional work remaining to be done, these risks exist and if they do, whether they are material to the global financial system. The FSB must meet that standard to support its policy recommendations.

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[116] For example, applying highly prescriptive liquidity requirements to a large number of funds could result in the homogenization of their portfolios and less diverse diversification. *See also*, Beale, *supra* note 115; Gaston Gelos, The Insurance Sector and Systemic Risk (July 27, 2016), *available at* http://voxeu.org/article/insurance-sector-and-systemic-risk (cautioning that in the insurance industry, systemic risk may arise from common exposures of a few large firms or many small ones); *See*, *e.g.*, Marco Cipriani et al., Gates, Fees, and Preemptive Runs, Fed. Res. Bank of N.Y. Staff Reps. (Apr. 2014), *available at* http://www.newyorkfed.org/research/staff_reports/sr670.pdf (warning that the imposition of gates and fees on mutual funds may be counterproductive); Fidelity-FSOC 2015 Letter at 12 (arguing redemption gates on funds investing in less liquid assets would have deleterious effect on small investors).

[117] Financial Innovation Now, Examining the Extensive Regulation of Financial Technologies, at 3 (July 2016), *available at* https://financialinnovationnow.org/wp-content/uploads/2016/07/Examining_the_Extensive_Regulation_of_Financial_Technologies.pdf; *see also id.* at 4 ("This system is supported by some incumbent players to benefit from anachronistic barriers to entry, and these entities may resist regulatory modernization. Some may even urge the adoption of additional and unnecessary burdens on innovative new entrants such as a federal safety and soundness regulatory regime like that imposed on banks and SIFIs - ignoring the fact that these new entrants pose no significant financial risk to taxpayers.").

[118] *See* Piwowar, *supra* note 10.

Fidelity would be pleased to provide any further information or respond to any questions that the FSB may have.

Sincerely,

cc: Jacob J. Lew, Secretary of the Treasury and Chairman of the Financial Stability Oversight Council
Thomas J. Curry, Comptroller of the Currency
Martin J. Gruenberg, Chairman of the Federal Deposit Insurance Corporation
Timothy Massad, Chairman of the Commodity Futures Trading Commission
Rick Metsger, Chairman of the National Credit Union Administration
Melvin Watt, Director of the Federal Housing Finance Agency
Mary Jo White, Chair of the U.S. Securities and Exchange Commission
S. Roy Woodall, Jr., Independent Insurance Expert, Financial Stability Oversight Council
Janet Yellen, Chair of the Board of Governors of the Federal Reserve System
Richard Cordray, Director of the Consumer Financial Protection Bureau
Richard Berner, Director of the Office of Financial Research
Michael McRaith, Director of the Federal Insurance Office
Adam Hamm, Insurance Commissioner, North Dakota Insurance Department
John Ducrest, Commissioner of the Louisiana Office of Financial Institutions and Chairman of the Conference of State Bank Supervisors
David Massey, Deputy Securities Administrator, North Carolina Department of the Secretary of State, Securities Division

Mark Carney, Chair, Financial Stability Board
Ashley Ian Alder, Chairman, International Organization of Securities Commissions
Paul P. Andrews, Secretary General, International Organization of Securities Commissions
Valdis Dombrovskis, Commissioner for Financial Stability, Financial Services and Capital Markets Union, European Commission

Kara Stein, Commissioner, U.S. Securities and Exchange Commission
Michael Piwowar, Commissioner, U.S. Securities and Exchange Commission