Fidelity Encourages the FSB and IOSCO to Abandon Their Proposal to Designate Investment Funds and Asset Managers as G-SIFIs

Fidelity Investments has filed a comment letter with the Financial Stability Board ("FSB") and the International Organization of Securities Commissions ("IOSCO") in which we encourage them to abandon the proposals to designate individual investment funds and asset managers as global systemically important financial institutions ("G-SIFIs"). We recommend that they instead analyze products and activities across the asset management industry and capital markets, similar to the approach that the FSOC and SEC are taking in the U.S. and that the IMF has endorsed internationally. Fidelity filed this comment letter in response to the Second Consultative Document that the FSB and IOSCO published on March 4, 2015.[1]

Background

On January 8, 2014, the FSB and IOSCO published their First Consultative Document, in which they proposed designating investment funds as G-SIFIs. The FSB and IOSCO recognized that asset managers do not exhibit the characteristics necessary to be G-SIFIs and excluded them from that proposal.[2]

Fidelity filed a comment letter responding to the First Consultative Document on April 7, 2014. We discouraged the FSB and IOSCO from pursuing designation as a means to analyze and regulate the asset management business. We explained that an individual fund or manager does not present the type and the scale of risk that SIFI designation was intended to address in banks. Further, we demonstrated that the high levels of substitutability and competition in asset management make designating an individual fund or manager an ineffective regulatory structure. We also provided evidence showing that funds and managers enter and exit the business regularly, in all market conditions, with no systemic impact.

The Second Consultative Document is materially worse than the First. The FSB and IOSCO appear to have ignored the comments they received on the First Consultative Document and in fact reversed their own positions on key points with which commenters agreed. They now propose designation not only of investment funds as G-SIFIs through a revised methodology that retains many of the flaws from the First Consultative Document; but they also seek to designate asset managers as G-SIFIs. These proposals ignore the economics, structure and existing regulation of the asset management business.

Summary of Fidelity's Comments

In Fidelity's comment letter on the Second Consultative Document we focus on mutual funds and their managers. We reiterate the points we made in our April 7, 2014 comment letter, which remain valid and unaddressed by the FSB and IOSCO. We also describe the jurisdictional and procedural failings of their proposals. Our main points are as follows:

- *The FSB and IOSCO are not required to develop a G-SIFI designation methodology for investment funds or asset managers, nor are they empowered to apply such a methodology to U.S. investment funds and asset managers*.

[1] Consultative Document (2nd): Assessment Methodologies for Identifying Non-Bank Non-Insurer Global Systemically Important Financial Institutions, available at http://www.financialstabilityboard.org/wp-content/uploads/2nd-Con-Doc-on-NBNI-G-SIFI-methodologies.pdf

[2] Consultative Document: Assessment Methodologies for Identifying Non-Bank Non-Insurer Global Systemically Important Financial Institutions, available at http://www.financialstabilityboard.org/wp-content/uploads/r_140108.pdf

- The FSB and IOSCO's mandate from the G20 did not direct them to develop G-SIFI designation methodologies for entities that do not present "SIFI" risk.
- Their own actions demonstrate that they are not required to develop these methodologies because they did not even propose one for asset managers in the First Consultative Document.

- *The FSB and IOSCO's G-SIFI designation proposal is the product of a defective rulemaking process and proposes a defective process for applying the G-SIFI methodologies*.
  - Their proposed methodologies appear to capture exclusively U.S. investment funds and asset managers, yet neither their rulemaking process, nor the procedures proposed for designating funds and managers, would meet the requirements of U.S. administrative or Constitutional law.
- *The FSB and IOSCO's proposals for G-SIFI designation of asset management entities are irredeemably flawed and should be abandoned*.
  - SIFI designation is intended to apply to entities that are "too big to fail." Designation serves no purpose unless (1) a company can fail and (2) its failure would disrupt global financial and economic activity so severely that policy makers and regulators are unwilling to allow it to fail through normal processes.
  - Mutual funds and their managers do not meet this test. Most operate with little or no leverage and are not susceptible to sudden failure like a bank. Furthermore, they are easily replaced by investors; and the evidence proves that they enter and exit the business regularly through normal processes with no systemic impact even during financial crises.
  - The proposed methodologies focus primarily on the size of funds and managers, despite evidence that size is not correlated to risk in asset management as it is in banking.
  - G-SIFI designation would fail to reduce systemic risk but it would harm funds, managers, investors and markets.
- *The proposed G-SIFI designation framework and methodologies for asset management entities do not apply to mutual funds or their managers specifically*.
  - The Second Consultative Document proposes a number of transmission channels, materiality thresholds and systemic importance indicators that do not fit the nature or basic features of mutual funds or the investor profile of mutual fund investors.
  - Asset managers do not pose systemic risk and designating one a G-SIFI would be counterproductive and destructive.
- *The FSB and IOSCO should shift to a products and activities analysis of the asset management industry and capital markets*.
  - The FSB and IOSCO are out of step with other regulators, academics and industry experts in failing to recognize that a products and activities approach is a more appropriate way to analyze and regulate the asset management industry and capital markets more broadly.
- *U.S. members of the FSB and IOSCO should reject the G-SIFI designation proposals*.
  - If the FSB and IOSCO continue to pursue G-SIFI designation of investment funds and asset managers and do not abandon these methodologies, U.S. members of the FSB and IOSCO should affirmatively reject them.
  - U.S. member agencies should focus instead on the process that the FSOC has begun, which the SEC should lead going forward, and on other more productive endeavors to analyze and regulate the capital markets.