

MEMO# 32557

June 26, 2020

Draft ICI Comment Letter on SEC's Fair Value Proposal-Comment Due by July 7

[32557]

June 26, 2020 TO: Accounting/Treasurers Committee
Chief Compliance Officer Committee
Investment Advisers Committee
SEC Rules Committee
Security Valuation Operations Committee
Small Funds Committee RE: Draft ICI Comment Letter on SEC's Fair Value Proposal-
Comment Due by July 7

In April, the SEC proposed new Rule 2a-5 under the Investment Company Act, which would address the fair value responsibilities of a fund's board and its adviser(s).[\[\[1\]\]](#) The proposal would:

- Establish specific valuation practices[\[\[2\]\]](#) for all funds to apply to portfolio investments that do *not* have readily available market quotations;
- Impose additional oversight and reporting obligations where a fund's board assigns fair value responsibilities to an investment adviser; and
- Rescind prior SEC and staff guidance on valuation and defer to existing accounting standards.[\[\[3\]\]](#)

Summary of ICI's Draft Comment Letter

ICI's draft comment letter (linked below) supports the SEC's fair value proposal because it more appropriately reflects the roles of fund boards, investment advisers, and accounting standards in funds' fair value determination process. We believe that with targeted amendments the SEC will be well-positioned to adopt a final rule that will benefit shareholders, funds, boards, and investment advisers.

We support the SEC's overall approach to this rulemaking. It rightly avoids providing comprehensive guidance about *how* funds should determine "fair value in good faith" for their wide array of portfolio investments, and instead focuses on process and allocation of fair value responsibilities.

We strongly support providing fund boards the ability to assign fair value responsibilities to investment advisers and rescinding prior SEC and staff valuation guidance. The proposal recognizes that a fund board's role is typically one of oversight, with the investment adviser (and other entities, including pricing services) establishing methodologies and doing the

day-to-day valuation work. And rescinding this SEC guidance in recognition of funds' reliance on existing accounting standards will provide greater clarity in this space by removing a potentially conflicting source of guidance.

To improve implementation consistent with investor protection, we recommend that any final rule:

- Reflect differences in fair value practices, risks, and challenges across asset types, and calibrate the requirements accordingly;
- More accurately capture the typical allocation of responsibilities between investment advisers and pricing services;
- Modify the frequency and content of the proposed board reporting requirements to better facilitate focused and effective board oversight, as boards and their investment advisers may mutually agree;
- Be a non-exclusive means of establishing statutory compliance (*i.e.*, a safe harbor), to recognize that funds do not “determine fair value in good faith” in a single way, and that such a flexible statutory requirement does not translate into a single and exclusive set of prescribed requirements.

Also, we:

- Support permitting sub-advisers to assume fair value responsibilities and recommend expanding the entities to which a fund board may assign these responsibilities;
- Recommend reaffirming that deviations in methodologies, inputs, and resulting fair value determinations will be inevitable across—and even within—fund complexes;
- Support leaving the type and frequency of testing to the fund's discretion and recommend clarifying that parties other than the adviser may perform testing;
- Recommend modifying the proposal's treatment of price challenges to focus on process rather than specific criteria;
- Support applying audit standards that permit sampling and other techniques to verify the values of securities owned;
- Recommend ensuring that this rule preserves funds' current ability to cross-trade certain securities; and
- Recommend adopting an 18-month compliance period.

Providing Feedback to ICI

Please provide any comments you may have on this draft letter to either or both of us (smith@ici.org or matt.thornton@ici.org) by Tuesday, July 7, COB.

Comments are due to the SEC by July 21, but we intend to submit this letter prior to that date.

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[Attachment](#)

endnotes

[\[\[1\]\]](#) Good Faith Determinations of Fair Value, SEC Release No. IC-33845, Apr. 21, 2020, available at: www.sec.gov/rules/proposed/2020/ic-33845.pdf.

[\[\[2\]\]](#) The proposal's general requirements under paragraph (a) would include: (i) periodically assessing and managing material risks associated with fair value determinations, including material conflicts of interest; (ii) establishing and applying fair value methodologies; (iii) testing fair value methodologies; (iv) overseeing and evaluating any pricing services used; (v) adopting and implementing written fair value policies and procedures; and (vi) satisfying recordkeeping requirements.

[\[\[3\]\]](#) See ICI [Memorandum](#) to Members No. 32409, dated April 23, 2020, for a detailed summary of the proposal.

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