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SEC Chair White Expects Continued 'Bright Spotlight' on Asset Management

The U.S. Securities and Exchange Commission (SEC) is contemplating several new initiatives governing registered funds, in addition to adopting rules this year on reporting modernization, liquidity management, and the use of derivatives, SEC Chair Mary Jo White announced at the opening session on the final day of ICI's annual General Membership Meeting (GMM).

"The spotlight on the asset management industry has been bright" since she joined the SEC as chair in 2013, she said, citing fund-related activity at the SEC, the Financial Stability Oversight Council, and the Financial Stability Board. White added that she expects this focus to continue in 2017 and beyond, as the industry continues to evolve to meet investor needs.

Speaking at GMM for the fourth time in as many years, White—the first career prosecutor and litigator to head the Commission—shared her "vision for the next steps in the evolution of regulation for the asset management industry." She described upcoming initiatives to address such issues as "disclosure effectiveness, the oversight of exchange-traded funds, accurate portfolio pricing, and cybersecurity, to name a few." She also described Commission efforts that will aim to address the form, content, and delivery of fund disclosures, including those related to fees and expenses.

Affirming a Risk-Focused Agenda for the Industry

During her tenure, the Commission's efforts related to asset management have been focused on developing "controls on specific fund portfolio composition risks and operational risk," White explained. Building on the three proposals now being finalized as rules, SEC staff members also are developing recommendations for proposals regarding transition planning and stress testing, the final two items in the regulatory agenda she set forth in December 2014.

White assured the capacity crowd that the SEC appreciated the "constructive suggestions" it had received from the industry and others on its proposed rules, and continues to welcome input. In talking about the Commission's liquidity risk management proposal, White acknowledged fund industry support for the overall concept, while citing industry concerns about the liquidity classification framework and the operational challenges for swing pricing. She reminded the audience that the SEC's responsibility is to ensure that funds and their advisers "use all of the tools necessary to effectively fulfill their legal responsibility to meet shareholder redemptions while minimizing the impact on remaining shareholders," a requirement that includes "a consideration of the kinds of products and strategies that are appropriate for mutual fund investments and investors."

White then briefly turned to the Commission's derivatives proposal, which she said is designed "to limit the amount of leverage that funds may obtain through the use of derivatives, and to require funds to implement derivatives risk management measures." After again welcoming commenters' general support for modernizing what she called an "outdated" regulatory regime, she acknowledged their concerns about the proposal's portfolio limitations, and described the range of suggested modifications and alternatives that some had offered.

Developing a New Disclosure Effectiveness Initiative

White revealed that, at her direction, the staff of the Division of Investment Management is in the early stages of a "disclosure effectiveness initiative" that she expects "will include ways to leverage advances in technology to improve the presentation and delivery of disclosures, and ways to enhance disclosure about fund strategies, investments, risks, and fees."

One element under consideration, she said, is whether improvements can be made to the fee table in prospectuses and summary prospectuses. The goal would be to "facilitate comprehension of the information [that the table] presents, and whether the most helpful information is required." She also encouraged industry input on a recommendation made in April by the SEC's Investment Advisory Committee to identify ways to improve mutual fund cost disclosure.

She said that other areas of focus in this initiative include:

- how funds can present risks most effectively;
- whether the requirement that a fund disclose certain factors that materially affect its performance can be improved; and
- whether additional improvements could be made to address "the concern about whether all of the information in a prospectus or statement of additional information continues to be necessary or helpful to investors."

A Further Look at ETFs and Cybersecurity

"The SEC's authority and focus go considerably beyond disclosure, and so should your focus and fiduciary decisionmaking," White continued, adding that "certain events over the last decade have sharpened our focus on particular types of funds that we believe require our enhanced attention." As an example, White cited exchange-traded funds (ETFs), saying that SEC staff members continue to review these funds in light of what they see as possible pricing and liquidity issues during the "flash crash" of May 2010, and turbulence in the market on August 24, 2015.

Staff members are examining the role of authorized participants and market makers, as well as the extent to which those players may affect liquidity in the markets, along with pricing issues and the ETF arbitrage mechanism, according to White.

She went on to caution funds about possible hurdles in their use of technology and service providers, as well as the need to be "adequately prepared to promptly and effectively respond to risks" related to cybersecurity.

White said funds must maintain "robust and responsible safeguards" for themselves and their investors. She noted that the SEC has been very active in the cybersecurity space, and is working to ensure that registered entities have appropriate policies and procedures in place. Admitting that no one can completely prevent disruptions from cybersecurity events, she said that fund managers should “consider the full range of cybersecurity risks to [their] funds, and consider appropriate tools and procedures to prevent breaches, detect attacks, and limit harm.”

Portfolio Pricing and Other Challenges for Funds

White also reminded attendees of the importance of accurate pricing by the services that assist fund managers with that function. “This is of high importance to everyone,” she emphasized. “I, along with your investors, expect that you will get it right.”

Other issues White encouraged fund providers to address included “fund governance, valuation, performance advertising, and issues that may arise when funds make payments to intermediaries for the distribution of fund shares.”

But for all the “challenges” that she cited, White ended the speech on an upbeat note, talking about the responsibilities that both the Commission and the fund industry bear. She called on asset management executives, “as the standard bearers” for the industry, to foster a culture in their organizations that “prioritizes responsibility and fairness, and asks first—and last—what is in the best interest of investors.”
