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Stevens Calls for Measures to Enhance Economic Growth

With America striving to achieve greater economic growth, Paul Schott Stevens, ICI president and CEO, called on the Securities and Exchange Commission (SEC) to enhance funds' essential role in the capital markets by proposing new rules to govern funds' use of derivatives and by creating a harmonized best interest standard for advisers providing investment advice to retail and retirement investors. The ICI chief also urged the SEC to adopt a fund disclosure regime for the 21st century.

In a breakfast keynote address at ICI's 59th annual General Membership Meeting (GMM), which wrapped up today, Stevens said that the US fund industry supports early steps by the Trump Administration to peel back layers of unnecessary and inappropriate financial regulation—a crucial part in the president's push for economic growth. Stevens provided critical context for this remark by observing that the fund industry has advocated efficient, effective regulation for more than 75 years, and that it embraces regulation as a necessary component to establish and build trust among investors.

SEC Plays a Role in the Promising Outlook for Financial Regulation

In light of President Trump's actions in his first 100 days, Stevens gave an "outlook for regulation that will improve prospects for our investors and our nation," though he warned that, this early in the administration, it is difficult to have clarity and certainty on financial proposals. Stevens offered ideas about how the SEC and its newly confirmed chairman, Jay Clayton, can help create an environment where millions of Americans can participate in and benefit from the capital markets. These suggested measures include:

- preserving the fundamental framework of fund regulation;
- ensuring that *all* investors—whether in retirement plans or retail accounts—have access to financial advice under a best interest standard;
- permitting funds to continue to use the most advanced investment tools and techniques; and
- bringing the fund industry's means of communications with shareholders into the 21st century.

Harmonized Best Interest Standard Will Help All Investors

"We are calling on the SEC to propose a harmonized best-interest standard for broker-dealers that would enhance, rather than replace, existing suitability obligations," Stevens said. He stressed ICI's support for "a requirement that all financial advisers act in the best interests of their clients—whether in retirement or retail accounts," adding that only the

SEC and Congress can lead the way in this effort. “We hope the SEC will take the lead—but if it doesn’t, Congress should stand ready,” Stevens said. He expressed the fund industry’s disappointment that the Department of Labor (DOL) had delayed the applicability date of its fiduciary rule by only 60 days—a decision that, he said, has already harmed investors.

“Yes, the rule takes effect on June 9—and prospects for further delay are uncertain,” he warned, highlighting the fact that hundreds of thousands of investors with small retirement accounts have already been “orphaned” and are being deprived of investment advice. “Faced with the sizable if uncertain legal and regulatory risks of assuming DOL fiduciary status vis-à-vis these fund shareholders, brokers are simply resigning from small accounts en masse”—unnecessary “carnage” that ICI predicted, Stevens said. “In the end, we believe the rule must be rescinded or significantly revised,” he concluded, explaining that it runs afoul of all the criteria that President Trump set forth in his directive to the DOL, which instructed the agency to review the rule.

Outline for a New Derivatives Proposal

In his call for SEC action, Stevens also highlighted the need to modernize decades’ worth of regulatory guidance on funds’ use of derivatives, and explained why the agency’s 2015 derivatives proposal falls short of that goal. Though ICI supports a mandate for funds to establish formal derivatives risk management programs and appropriately tailored asset segregation requirements, he said, the initiative’s proposed portfolio limits and other overly restrictive provisions “would sharply—and excessively—restrict funds’ use of derivatives.”

Echoing concerns ICI expressed to the SEC in response to the agency’s 2015 proposal, Stevens stressed that the proposal’s portfolio limits could stop funds from using instruments that reduce risk and improve liquidity—driving the funds to deregister, or depriving investors of core strategies. The fund industry must protect investors’ “access to the best and most efficient portfolio management we can offer,” Stevens said, calling for the SEC to start afresh with a proposal that would maintain funds’ ability to use derivatives as a portfolio management tool. Such an approach will “encourage funds to invest in the derivatives market confidently and responsibly—to the ultimate benefit of their investors.”

Bringing Fund Disclosure into the 21st Century

Stevens continued the Institute’s advocacy for the SEC to “bring fund disclosure into the 21st century.” He recalled that the SEC came close to improving online delivery of fund shareholder reports, in a 2016 proposal that the agency has not adopted. “Now, we urge the new Commission to adopt a three-stage process for bringing fund disclosure into the 21st century,” he said, noting that 92 percent of US mutual fund–owning households have access to the Internet. Stevens suggested this process:

- The SEC should immediately adopt a rule that allows mutual funds, exchange-traded funds (ETFs), and closed-end funds to meet their delivery obligations by posting required disclosure documents online, and providing investors the opportunity to opt for paper.
- At the same time, the SEC should permit variable insurance products to develop and use summary prospectuses, delivered online.
- As a longer-term initiative, the Commission should review the content of fund shareholder reports to make them more useful to investors.

Preserving the Framework of Fund Regulation

Looking back to former SEC chair Mary Jo White’s asset management agenda—which affirmed the SEC’s role as the industry’s primary regulatory—Stevens praised steps by the

Trump Administration and the leadership in Congress to remove the threat of inappropriate, bank-like regulation by the Federal Reserve for registered funds. He applauded President Trump's directive to Treasury Secretary Steven Mnuchin in April to block designation by the Financial Stability Oversight Council (FSOC) of nonbank financial institutions as systemically important financial institutions (SIFIs), pending a thorough review of FSOC's designation process.

Stevens added that ICI supports the objective of the Financial CHOICE Act to revoke the FSOC's authority under the Dodd-Frank Act to designate non-banks as SIFIs—including funds and their managers. Noting that the House Financial Services Committee approved the bill on May 5, he expressed hope that "this Congress can address the dangers that SIFI designation poses for our industry."

Sensible Regulation That Avoids "Check-the-Box" Regulation

In a post-speech question-and-answer session with GMM Planning Committee Chairman James McNamara, president and CEO of Goldman Sachs Mutual Funds, Stevens advised the SEC to "move on" rather than pursue a proposed rule to require funds to adopt business continuity plans. Funds, in keeping with business and investor imperatives, already operate such plans in conformance with SEC guidance, he explained.

Similarly, Stevens rejected the concept of an SEC rule to mandate stress tests for funds, despite a directive to the Commission in the Dodd-Frank Act to adopt such a rule. This provision was driven by a post–financial crisis focus on the banking sector, he explained. "I don't know what stress testing would look like for funds," Stevens said, adding that he wonders whether the SEC knows either.

Stevens also raised the issue of inadequate cybersecurity protection by the SEC for the "continuous feed" of market-sensitive, feed" of market-sensitive, monthly data that funds will soon report under the Commission's new data-reporting rule. As ICI has told the SEC, until the SEC provides a higher level of cybersecurity protection, a better approach would be to require quarterly, rather than monthly, disclosure of fund data under the rule. ICI will continue to work on the issue with the agency, he said. In the meantime, ICI continues to assist members in efforts to reinforce their own cybersecurity systems, Stevens noted, by providing committees and other forums where cybersecurity experts from member companies can share information about threats and solutions.

Stevens also examined another a risk-reducing initiative by ICI. Together with the Securities Industry and Financial Markets Association and the Depository Trust & Clearing Corporation, the Institute has led the push to transition to a shorter securities settlement cycle, moving from transaction date plus three days (T+3) to T+2. Stevens expressed his appreciation to the SEC for passing new rules to enable this move, and called on the Office of the Controller of the Currency and the Federal Deposit Insurance Corporation to follow suit and conform their rules to the SEC's. The agencies need to move quickly on this, he said, given that the scheduled implementation date for the move to T+2 is September 5.

The Benefits of Consensus at the SEC

Asked for comment by McNamara about his hopes for an SEC with a new chairman and new members, Stevens recommended that the agency work to achieve consensus on its agenda. In light of past divisions in regulatory and policymaking bodies throughout the city, he expressed a wish that "everyone in Washington would wake up each morning and say, 'I need to do something to day to get our country moving.'" This, he suggested, would be transformative and open a path to economic growth in America, helping to realize the promise of the nation for everyone.

Summing up the fund industry’s reaction to the first 100 days of the Trump Administration, Stevens said, “We are pleased by what we’ve seen on financial regulation—the executive orders, the presidential memoranda, the declarations by nominees, and the tide on Capitol Hill. Most of all, we are pleased by the emphasis on regulation that serves investors and the economy—rather than regulation for its own sake.”

“We are prepared to work as long as is necessary to restore balance to our financial system, so that our country can unleash its entrepreneurial and innovative powers,” Stevens pledged. “ICI and its members look forward to that challenge.”
