

ICI President's Address, 2023 Investment Management Conference

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“Celebrating the Mutual Fund and the Appropriate Role of Regulation”

Thank you, and good morning.

I'm grateful to Terry Nilsen for kicking us off, and I'm glad to welcome all of you to the ICI Investment Management Conference. For those of you who were here last year, it's great to see you again. And it's just as great to see so many new faces. We're glad you're here!

It's always a pleasure to address members of the most important industry in finance. And it's a privilege to be joined today and tomorrow by so many leaders from the Securities and Exchange Commission.

At this conference, we'll hear from Commissioner Mark Uyeda and SEC staff from the Divisions of Investment Management, Enforcement, and Examinations.

And of course, as soon as I'm done speaking, we'll hear from the *Director* of the Division of Investment Management, William Birdthistle. I know one of the highlights of this conference is hearing directly from the regulators, and we're all excited for Director Birdthistle's remarks.

Our capital markets are the envy of the world, creating countless opportunities for individual long-term investors to achieve their financial goals. That theme will run through everything you hear over the next few days, and, more importantly, it will define everything we do as an industry moving forward. We must keep our markets vibrant, while expanding the good they do and the difference they make for the American people.

Our capital markets connect hundreds of millions of investors with companies of all sizes. What's more, they direct hundreds of *billions* of dollars to their highest use, turning small businesses into big ones and making successful companies even better. Our capital markets find and fund the next American success story, day after day, and they make America itself the most successful economy in human history.

Mutual funds are at the heart of this progress. They are the original and greatest democratizing force in the investing space, and to this day, they give people unprecedented access to the capital markets. All told, more than 100 million Americans, most of them middle-class, depend on mutual funds to achieve their savings goals, from education to homeownership. And as we all know, mutual funds are especially important for retirement. For the great majority of Americans, the mutual fund is the *cornerstone* of their secure financial future.

The importance of the mutual fund is further bolstered by the innovation that has gone into them. Our industry has gone to extraordinary lengths to give investors access to affordable, diversified, and professionally managed portfolios, and through fierce competition we're constantly looking to expand both accessibility and affordability. Thanks to the hard work of the people in this room and across the country, we've made great headway.

Look no further than fund fees and expenses, which have plummeted for decades. In fact, in the 25 years between 1996 and 2021, average expense ratios for equity mutual funds and bond mutual funds have fallen by more than half. It's a record that few products or services in the US economy can match.

At the same time, our industry has expanded the range of products we offer investors. Consider, for instance, target-date funds, which are particularly popular among younger 401(k) plan participants, because they offer convenience and instant diversification. It is safe to say that investors have an abundance of choice, with the ability to select from a diverse universe of products and strategies that are best suited to meet their financial objectives.

We should recognize this progress, and yes, we should celebrate it. For that matter, we should ask ourselves what we can do to keep moving forward. That includes a discussion of the policies that will do the most good for the most people, as well as critiquing the rules and regulations that risk *hurting* investors and *holding* back progress.

This is the focus of the bulk of my remarks, as it's top of mind for our entire industry. I hope our policymakers fully appreciate the special role that mutual funds play in our capital markets and the lives

of American investors. I hope they recognize that mutual funds are essential and irreplaceable in securing a financial future for so many.

I do worry, however. It sometimes appears that policymakers favor a bank-centric prudential regulatory view toward the capital markets, which translates into looking for ways to eliminate as much risk as possible from the financial system. But this approach is inconsistent with the historical regulatory approach that has worked so well for so long. Consider, for example, the US regulatory regime's traditional reliance on regulatory tools like disclosure, which explicitly recognizes the risks inherent in investing.

Applying a bank prudential regulatory lens to our capital markets will harm far more people than it helps. Different levels of risk and risk pricing are implicit within investment markets, and trying to eliminate risk will stifle the progress that investors deserve and what our capital markets depend on. More to the point, it will limit access to returns generated by mutual funds, holding back the progress we hope to deliver for an even greater share of Americans.

Some of this trend comes from regulators' belief that American financial markets should adopt what is done in other jurisdictions, like those in Europe. We should be careful. While we should be open to good ideas from any corner of the world, we also should continue to appreciate the strengths and unique characteristics of our markets and the regulatory approach that supports them.

The fact is that countries in Europe and Asia often look to the US for inspiration. They envy our vibrant capital markets and look to move their own economies away from relying so much on bank financing. They dream of giving their citizens the same level of investment opportunities that the average American enjoys today.

That's why I'm so concerned that regulators are at risk of limiting Americans' investment options. And, to this end, I have serious concerns with the pace and scale of the SEC's current agenda. The Commission has issued a slew of rule proposals on a wide range of topics where much more work needs to be done to understand their cumulative effect on the markets and investors. Many of the rules also seem to be fall into the category of solutions in search of articulated problems.

One example is the proposed Fund Names rule amendments rolled out last year. The current version of this rule has worked well for decades, and it reflects the principle that while a name helps an investor choosing from an array of funds, it's the starting point, not the last word. The proposal, however, tries to make a fund's name do far too much, and ironically, it may cause investors to place too much reliance on a few words that describe a financial product.

This policy choice is puzzling, given the SEC's focus on improving disclosure for investors by creating short documents with essential information such as a fund's investment strategy and performance. That information can easily be accessed in SEC-mandated summary prospectuses and streamlined shareholder reports. So why shoehorn so much into the fund name, as well?

By the SEC's own admission, complying with this mandate will cost as much as \$5 billion. That's an astronomical sum, especially for a rule with a less-than-clear rationale, and it's a price tag that investors should *never* have to pay.

The same is true for the SEC's proposed rule on "Outsourcing by Investment Advisers." If adopted, it would create burdens on investment advisers without creating any additional protections for investors. That's a damaging combination.

Other proposals raise similar concerns. Yet the most worrisome of all is the SEC's latest proposal on mandatory swing pricing, hard close and liquidity risk management. The proposal is breathtaking in scope, and it's no exaggeration to say that it represents the most significant transformation of the mutual fund industry in generations.

Such a sweeping mandate requires the strongest possible justification and the longest possible drafting and review process. Yet in our view, the proposal is not sufficiently attuned to its impact on the hundred-million-plus investors who depend on mutual funds for their financial security.

The ICI made this clear to the SEC in a formal comment letter we submitted last month. We devoted 180 pages to in-depth legal and economic analysis, and I'll describe three particular areas of concern.

First, in our opinion, the SEC did not adequately explain and quantify the problem it's trying to solve. Instead, the proposal just generally invokes the concepts of dilution and resiliency. It's missing a comprehensive analysis of the landscape and investor experience, which is necessary to justify such a massive shift in regulation and such a massive burden on mutual funds, intermediaries, and investors.

On that note, our second concern is that the SEC is not accounting for the sizeable compliance costs this mandate will impose. Small- and mid-size mutual funds, which typically have the least financial resources, are most at risk. As their costs go up, so will prices for investors. And in some cases, rising compliance costs will sink mutual funds, leaving investors with fewer choices and less competition.

Our third concern is centered on dilution. While the SEC cites dilution as a primary reason for this proposal, ICI has found that, depending on the fund type, dilution ranges from minimal to non-existent. We estimate that daily dilution for U.S. mutual funds is typically just hundredths or tenths of a basis point per day. Over the longer-term, any potential dilution would be greatly offset by the returns investors earn from such mutual funds. The data simply do not support the SEC's sledgehammer-like approach.

Consequently, targeted reforms are a far better approach than any one-size-fits-all plan. Fixing clearly identified problems is far superior to inadvertently creating bigger problems across the entire mutual fund market.

It's hard to overstate how harmful those problems will be. If this mandate moves forward, middle-class Americans will be at a severe disadvantage in our country's financial markets. To start, the rule would

make it difficult or impossible for regular investors to trade and receive timely pricing in response to market events. These changes will leave investors with less control over their investments and the benefits they provide.

Middle-class investors on the West Coast would be hit even worse – discriminated against purely due to their time zone. They would be permanently behind investors on the East Coast and the center of the country. In fact, the cut off for daily trading would likely come before most people on the West Coast even get out of bed. That’s 50 million or more Americans at risk of being left behind – every single day.

There is much more I could say about the proposed swing pricing, hard close and liquidity risk management rule. Fortunately, many others are saying the same things. To date, the SEC has received more than three thousand comment letters on this proposal – and most express deep concerns.

It’s one of the most commented-on SEC proposals last year, and much of the feedback is coming from the very retail investors who will suffer under it. Criticism is also coming from organizations representing a diverse range of market participants and perspectives, including the College Savings Foundation, Better Markets, the American Retirement Association, and the SPARK Institute.

The SEC even received a joint letter from Republican Ann Wagner and Democrat Brad Sherman, the Chair and Ranking Member of the House Financial Services Committee Subcommittee on Capital Markets. They expressed concerns about the impact of this proposal on individual investors. It turns out that opposition to this proposal unites Congress across party lines. That’s quite a statement in these divided times.

Across the board, stakeholders are making clear: This is not the direction we should be going, nor is it the direction our industry has taken. For decades, we’ve strived to deliver lower costs, more options, and greater flexibility, with remarkable success. Our progress is evident in the more than 100 million Americans who’ve entrusted mutual fund managers with their hard-earned money, and we’re taking steps to reach a new and even more diverse generation of investors.

The SEC has overseen the growth and development of the US capital markets that helped to support an American middle class. Since its founding, the SEC has kept watch while retirement and financial security became attainable goals for tens of millions of people from all walks of life. Its mission is uniquely American, focusing on the disclosure and truth before all else, and carefully considering the people that rely on the financial products they regulate.

But the SEC’s current approach stands in contrast to its history. Let me be clear: ICI has always been, and always will be, a strong supporter of thoughtful, measured policy. It’s in our DNA. We have an 80-plus-year track record of supporting regulations that improve the market and protect investors. We also have a duty to share our perspective and expertise to move policies in a better direction.

That's exactly what we're doing now. We will continue to engage on these critical matters in good faith. We trust that the SEC will as well. Despite our current differences of opinion, we hold the SEC and its staff in the highest regard and know that they bring great talent and professionalism to their very challenging work. We promise to do the same, in a spirit of conversation and collaboration.

This is my hope coming out of conference – that the private and public sector can unite in common cause and continued progress. Let's work together to help more investors save for education, homes, and retirement. And together, let's make our country's capital markets even stronger than they already are – lifting up everyone, from all walks of life.

As an industry, we want nothing more. And I know we all agree that the American people deserve nothing less.

Thank you. And once again, welcome to the Investment Management Conference.

It is now my privilege to introduce our next speaker.

William Birdthistle is the Director of the Securities and Exchange Commission's Division of Investment Management. In his role as Director, Mr. Birdthistle oversees the Division's overall operations, core functions, and mission.

Prior to joining the SEC in 2021, Mr. Birdthistle was a professor of law at Chicago-Kent College of Law, where his scholarship focused on investment funds, securities regulation, and corporate governance.

Since becoming IM Director, Mr. Birdthistle has hit the ground running and has become well-known to the industry. I appreciate Mr. Birdthistle being here and taking the opportunity to speak directly to the leading legal and compliance professionals of the fund industry.

[To Birdthistle] Thank you for being here. We look forward to hearing your perspective and insights.

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