January 4, 2021

By Electronic Submission

Secretary
Securities and Exchange Commission
100 F Street NE
Washington, D.C. 20549-1090

Re: SEC File Number S7—09—20[1]

To Whom it May Concern:

The Index Industry Association[2] (IIA, or we) appreciates the opportunity to comment on the Securities and Exchange Commission's (SEC) proposed rule regarding Tailored Shareholder Reports (File Number S7—09—20) (hereinafter, Proposed Rule).

The IIA is an independent, not-for-profit organization composed of leading global, independent index administrators.[3] We work with market participants, regulators, policymakers and other representative bodies to promote sound indexing practices that strengthen markets, serve the needs of investors and educate market participants. Our members are independent index administrators, meaning none of our members trade the underlying component securities of their indices nor do they create investment products for investors. This model mitigates real and perceived conflicts of interests. Our Best Practice Guidelines (Guidelines)[4] are designed to ensure the highest quality and integrity of indices administered, maintained, or calculated by index providers and foster continuous improvement, innovation, and vigorous competition in all aspects of the index industry. The Guidelines focus on independent governance of index methodologies, transparency, accountability, data collection, and quality index calculation and validation. They include standards for addressing conflict of interest, business continuity, confidentiality, record-keeping, handling complaints, and internal controls.

As discussed in the Proposed Rule, the SEC has long required funds to disclose a comparison of their performance against a broad-based market index in fund reporting materials. The IIA sees no reason to change this approach and believes that the disclosure of fund performance relative to a broad-based market index promotes transparency and provides shareholders important metrics to evaluate their goals. We also agree that benchmarking fund performance against more tailored indices as an additional measurement can provide shareholders additional useful information. Given the importance of providing accurate information to stakeholders, index providers employ robust due diligence standards. The IIA believes that the International Organization of Securities Commissions' (IOSCO) Principles for Financial Benchmarks (IOSCO Principles) and existing SEC rules are thoughtful measures that address governance, due diligence, and other issues effectively.

---

[1] The "Tailored Shareholder Reports, Treatment of Annual Prospectus Updates for Existing Investors, and Improved Fee and Risk Disclosure for Mutual Funds and Exchange-Traded Funds; Fee Information in Investment Company Advertisements" proposed rule (RIN 3235-AM52).
[2] Please see our website at http://www.indexindustry.org/.
[3] For a list of members, please see http://www.indexindustry.org/about-iia/.
[4] Please see our website at http://www.indexindustry.org/advocacy/.

Management's Discussion of Fund Performance

The context of overall market performance is critical to enabling shareholders to evaluate the performance of any individual fund because it allows shareholders to consider adequately the opportunity cost of their investments. The performance of the overall market as represented by indices is also the most readily understood reference point for many investors to help interpret and assess the historical performance profile of a particular fund, and help monitor the success of an investor's portfolios relative to her investment objectives. Broad-based market indices make such evaluations possible, reliable, and useful.

Given the wide range of investment opportunities and the complexity of modern capital markets, shareholders may also benefit by funds' use of secondary benchmarks as an additional, and more specific, measurement of fund performance. In particular, it is appropriate for a fund to compare its performance to a secondary benchmark that matches the investment thesis or risk exposure characteristics of that particular fund. Evaluating the performance of a fund against a more tailored benchmark would offer an apples-to-apples comparison, thereby providing shareholders more relevant information about a fund's success relative to its specific investment mandate.

We acknowledge concerns about the potential costs associated with the disclosure requirement, but we do not believe the Proposed Rule's clarification to use a broad-based market index should result in any meaningfully increased costs.[5] For the merely comparative uses of an index that are at issue here, such as publication of charts and graphs in a fund's reports, index providers typically charge proportionately low fees. Thus, most funds incur a small, competitive fee in the course of measuring their performance relative to a broad-based or a more tailored index. Moreover, index values obtained for the purpose of creating charts and graphs to satisfy fund reporting requirements are often readily accessible. Also, the fees associated with the commercialization of indices as a basis of passive investment management strategies are a small part of an index-based fund's overall costs, as such fees are often linked proportionally to the fund's size (e.g., its assets under management).[6]

Index Governance

We appreciate the SEC's interest in the due diligence, governance, and related standards relating to indexes in light of the ways that funds use indexes to benchmark their performance and as a basis for indexed investments. IIA members follow best practices and international standards to ensure the integrity and transparency of benchmark determination processes.

As previously mentioned, the IIA has developed Best Practice Guidelines that funds and asset managers can take into consideration when conducting due diligence in selecting an index and on-going monitoring of the index provider. Guidelines focus on independent governance of index methodologies, transparency, accountability, data collection, and high quality index calculation and validation. They include standards for addressing conflict of interest, business continuity, confidentiality, record-keeping, handling complaints, and internal controls. Under these Guidelines,

[5] The Proposed Rule also notes critiques of the argument that that index licensing fees can be costly to funds. See 85 Fed. Reg. 70716 70741 (Nov. 5, 2020).

[6] Additionally, the costs associated with an index-based fund are low compared with fees associated with active management. According the Investment Company Institute, as of December 31, 2019, the average active equity mutual fund in the U.S. charges investors 76 basis points. By comparison, the average index equity fund charges 8 basis points. See https://www.callan.com/wp-content/uploads/2019/12/Callan-2019-IM-Fee-Study.pdf.

members must establish Governance Bodies to oversee the administration, calculation and maintenance of indices, including oversight of relevant employees and service providers. IIA members also establish policies and procedures to identify, monitor, and resolve material deficiencies in their work quickly as well as policies to mitigate any existing or potential conflicts of interest, among many other best practices to promote index transparency and accuracy.

In addition to these best practices, the index provider industry complies with the IOSCO Principles, due in part to the SEC's leadership.[7] IOSCO's stated objective in creating the IOSCO Principles was to establish policy guidance and principles for index-related activities that would address conflicts of interest and promote good design and robust transparency. Under the IOSCO Principles, index providers' governance and control frameworks are multifaceted so they can protect the integrity and quality of their indices. For instance, index providers are expected to separate commercial functions from operational and analytical functions into distinct reporting lines, and to establish a control framework to support a sound process for developing, calculating, and distributing indices, among other safeguards.

We also note that the SEC has implemented effective rules and guidance regarding the obligations of registered funds, their boards of directors, and investment advisers to conduct due diligence on and to monitor their service providers. For instance, ICA Rule 38a-1 requires funds to adopt and implement written compliance policies and procedures reasonably designed to prevent violation of the federal securities. Additionally, Rule 206(4)-7 requires registered investment advisers to adopt and implement written policies and procedures reasonably designed to prevent violation of the Advisers Act by the adviser or any of its supervised persons.

In times of crisis, such as the current pandemic, these best practices, the IOSCO Principles, and SEC rules have helped index providers operate effectively.

Conclusion

We agree with the SEC that comparing fund performance against a broad-based market index in fund reporting materials promotes transparency and helps shareholders evaluate their goals. We also believe fund regulation, industry best practices, the well-developed IOSCO Principles have brought a stronger, more consistent approach to index industry governance.

We appreciate the opportunity to comment on the Proposed Rule and commend the SEC for its work. We would be happy to meet with you to discuss our comments and provide further detail.

Sincerely,

/s/Rick Redding
Rick Redding
Chief Executive Officer
Index Industry Association

[7] Many of the IIA's members adhere to the IOSCO Principles, including by making available public statements of adherence with detailed descriptions of their control frameworks to funds and asset managers conducting due diligence and engaging an independent third-party auditor to examine compliance with the IOSCO Principles.