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September 2, 2016

VIA E-MAIL RULE-COMMENTS@SEC.GOV

Mr. Brent J. Fields

Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Adviser Business Continuity and Transition Plans (File No. S7-13-16)

Dear Mr. Fields:

This letter presents the comments of Federated Investors, Inc. and its subsidiaries ("Federated") with respect to the recent issuance by the Securities and Exchange Commission (the "Commission") of a release (the "Release") proposing new regulations that would require registered investment advisers to adopt and implement reasonably designed business continuity ("BC") and transition plans (the "Proposed Rule").[1] Federated is one of the largest investment management firms in the United States (the "U.S."). Federated's advisory subsidiaries managed $255 billion in money market assets and $367.2 billion in total assets as of June 30, 2016. As investment adviser to 123 registered funds and a variety of separately managed account options, Federated provides comprehensive investment management to more than 8,400 institutions and intermediaries including corporations, government entities, insurance companies, foundations and endowments, banks and broker/dealers.

While we acknowledge the potential benefits of some elements of the Proposed Rule, Federated opposes the Proposed Rule in its current form.[2]

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1 Adviser Business Continuity and Transition Plans, Exchange Act Release No. IA-4439, 81 Fed. Reg. 43,530 (July 5, 2016).

2 We also support many of the comments made by the Investment Company Institute on the Proposed Rule in its comment letter dated August 23, 2016. For example, among others, we agree with the Investment Company Institute that: (i) the Commission should issue guidance under Rule 206(4)-7 under the Investment Advisers Act of 1940 instead of adopting a new rule; (ii) the Commission should avoid language suggesting that BC plan or transition-planning violations (as determined by the Commission) would be per se fraud or deceit; (iii) an investment adviser's obligation should be to "mitigate," rather than eliminate, risks of operational disruptions; (iv) the Commission should acknowledge that certain limits exist on an investment advisers' oversight of vendors' BC plans and ability to change vendors; and (v) any rule or guidance on transition planning should

1. **BC Plans.** Federated agrees with the need for an updated framework to strengthen industry practice, but we believe that the Release: (i) sets an unreasonable standard for advisers that is not justified by cost/benefit assessments; (ii) fails to acknowledge the obstacles advisers face due to the inability of critical service providers to provide adequate clarity regarding their BC programs because of the service providers' need for confidentiality (thus requiring greater redundancies by investment advisers under the Proposed Rule); and (iii) fails to acknowledge and clarify the important role of disclosure in informing investors of the risks associated with BC events. At this stage, additional guidance under rule 206(4)-7 under the Investment Advisers Act of 1940 is appropriate rather than a new rule.

2. **Transition Plans.** Federated believes that the Proposed Rule for transition plans: (i) is highly burdensome while having little practical value as it requires meaningless speculation by the adviser regarding transactions it may undertake in hypothetical risk scenarios; (ii) is not cost/benefit justified based on the historical experience of advisers of registered vehicles that would be most affected by the Proposed Rule; and (iii) creates a record to assist in regulatory oversight that could alternatively be achieved by far simpler and less costly means.

Set forth below is a summary of our specific comments and suggestions with respect to the Proposed Rule. We also set forth our responses to the specific questions posed by the Commission in the Release.

I. Business Continuity Plans

Federated appreciates that the need for more uniform BC preparedness across the investment management industry. We believe, however, that the Proposed Rule would be an inappropriate and ineffective means of achieving that objective; and that additional guidance under rule 206(4)-7 would be appropriate.

1. The Proposed Rule creates an unreasonable standard for adviser BC plans.

Although the Proposed Rule states the requirement that adviser BC plans must be *reasonably designed to address operational and other risks related to a significant disruption of an adviser's operations*,[3] language throughout the Release suggests that the adviser is expected to be the *de facto* guarantor of any cyber or business interruption that has an adverse impact on client accounts. For instance, the Release states:

> Because an adviser's fiduciary duty obligates it to take steps to protect client interests from being placed at risk as a result of the adviser's inability to provide advisory services, clients are entitled to assume that advisers have taken the steps necessary to protect those interests in times of stress, whether that stress is specific to the adviser or the result of broader market and industry events. We believe it would be

take a "general playbook" approach and not require cataloging of every possible contingency or development of a distinct BC plan for every fund (or client).

[3] Adviser Business Continuity and Transition Plans, *supra* note 1, at 43,532.

> fraudulent and deceptive for an adviser to hold itself out as providing advisory services unless it has taken steps to protect clients' interests from being placed at risk as a result of the adviser's inability (whether temporary or permanent) to provide those services.[4]

This creates an extraordinary standard of care as the adviser is expected to protect against any broad market or industry events regardless of origin. The Release continues:

> As discussed above, an adviser's fiduciary obligations require it to take steps to protect its clients' interests from being placed at risk as a result of the adviser's inability to provide advisory services. This fiduciary duty fosters trust between the client and its adviser, such that the client relies on the adviser to act in its best interests and safeguard its assets as appropriate, even during times of stress. If an adviser is unable to provide advisory services after, for example, a natural disaster, a cyber-attack, an act of terrorism, technology failures, or the departure of key personnel, its temporary inability to continue operations may put clients' interests at risk and prevent it from meeting its fiduciary duty to clients. This risk could include the risk of loss if, for example, an adviser lacks the ability to make trades in a portfolio, is unable to receive or implement directions from clients, or if clients are unable to access their assets or accounts. As part of its fiduciary duty to protect client interests, an adviser also should take steps to ***minimize*** operational and other risks that could lead to a significant business disruption like, for example, a systems failure. In order to do so, advisers should generally assess and inventory the components of their business and minimize the scope of its vulnerability to a significant business disruption.[5]

The requirements expressed above are not qualified by a reasonableness standard, but are absolute as the adviser must *minimize* operational and other risks arising from events such as natural disasters, cyberattacks or acts of terrorism. In just one oblique reference the Release acknowledges that advisers may not be able to prevent all disruptions:

> While we recognize that an adviser may not be able to prevent significant business disruptions (e.g., a natural disaster, terrorist attack, loss of service from a third-party), we believe robust planning for significant business disruptions can help to mitigate their effects and, in some cases, minimize the likelihood of their occurrence.[6]

In its totality, however, the Release states that the adviser will be expected to prevent or "minimize" any harm to clients as a result of those disruptions.

The Proposed Rule therefore creates an unreasonable standard for advisers. In developing BC plans that are *reasonably designed* to mitigate the adverse impacts of internal or external disruptions, advisers can only defend against events that can be *reasonably anticipated* and should not be subjected to the 20/20 hindsight of Commission examiners or civil litigation. Furthermore, such safeguards must entail reasonable and fair expense within the context of the adviser's business and fees charged for the adviser's services. In particular, it is unreasonable to expect that an adviser could economically create stand-by BC facilities that effectively in-source all of the third-party services that had been outsourced to large service providers such as custodians, transfer agents, accountants and trade execution facilities. The first principles of cost/benefit analysis make it clear that advisers must be permitted to calibrate their BC plans to the nature, size and scope of their advisory services, as well as the fees charged for building and

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4 *Id.*
5 *Id.* at 43,534 (emphasis added).
6 *Id.*

supporting costly infrastructure. Whether embedded in a final rule, or as guidance under rule 206(4)-7, it must be made clear that BC plans should be "reasonably designed," do not serve as guarantees by advisers against every client harm in every circumstance, do not require advisers to implement unfeasible or cost-prohibitive measures to meet the standards, and will not serve as the basis for administrative or civil proceedings so long as an adviser acted in good faith to adopt and implement a reasonably designed BC plan.[7]

2. **It is premature to enact a rule given the evolving understanding of realistic standards for advisers and the inability of critical service providers to disclose their BC programs in adequate detail.**

Much of the Proposed Rule focuses on continuity risks associated with critical services provided to mutual funds and other investment vehicles. At the present time, the asset servicing industry does not adequately or uniformly respond to requests by advisers for information regarding their BC or information security programs. This reluctance is primarily attributable to the concerns of asset servicing firms that such information is confidential and the disclosure of such information could expose them and their customers to cyber or other threats. In light of this concern, the Proposed Rule would subject advisers to the unreasonable burden of establishing additional and redundant continuity plans owing solely to the inability of service providers to demonstrate existing safeguards adequately. The Commission should work with the industry to develop standards and uniform attestations, such as SOC 2s, that would enable advisers to develop a more informed assessment of the residual continuity risks that must be addressed by the advisers' BC plans.

Furthermore, the industry is rapidly evolving with larger complexes that provide mutual funds having a generally more advanced state of readiness than smaller advisers. The Proposed Rule provides little or no context for how advisers of differing sizes may calibrate their BC programs to the circumstances of their individual operations. While we believe that all advisers must carefully consider their exposure to cyber and other business interruption risks and develop BC programs to address these risks, the Proposed Rule would create an unreasonable barrier to entry for small or new advisers, thus thwarting competition in the industry.

Given the evolving understanding of realistic standards, and the disclosure limitations of service providers, it is strongly recommended that the Commission forgo rulemaking at the

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[7] It must also be emphasized that the cost estimates provided by the Release are highly unrealistic. Footnotes 124 and 132 of the Release summarize the Commission's estimated costs of complying with the Proposed Rule (for both BC and transition planning) at: (i) \$30,000 to \$1,500,000 per adviser for initial costs; and (ii) \$7,500 to \$375,000 per adviser for ongoing costs. *Id.* at 43,548 n.124; *id.* at 43,549 n.132. These costs may be realistic to physically create the actual documents, policies and procedures that constitute the plans. The majority of the costs, however, are personnel expenses in creating and maintaining BC departments; business unit personnel expense in working with BC departments to create and regularly test BC plans; additional software and data licensing requirements; additional physical locations; and the costs to design and implement additional back-up electronic systems that would be used during potential BC events. For a large investment adviser, the additional expense necessary to comply with the Proposed Rule could be \$15,000,000 or more, which is an order of magnitude greater than that estimated by the Commission.

present time and issue guidance under rule 206(4)-7 to complement recent guidance under rule 38a-1 under the Investment Company Act, and allow time for industry practice to mature. An overarching rule can be enacted at a later stage, if warranted, that would be better informed by the practical limitations that the industry will encounter in developing BC programs and working with critical service providers.

3. **The Release fails to establish any role for disclosure in alerting investors to BC risks that may not be addressed by the adviser's BC program.**

The presumed intent of the Proposed Rule to require that advisers protect their clients against losses created as a result of any BC events is further evidenced by the failure of the Release to provide any role for prospectus and brochure disclosure in alerting fund investors and advisory clients to the risks associated with unavoidable or unforeseeable business disruptions. As with any other material risk, advisers should be required to disclose the existence and potential repercussions of BC risks, the existence of their BC plans and other efforts to mitigate these risks, and the existence of certain unavoidable risks that may result from systemic events that are unavoidable and other risks against which the adviser cannot economically defend.

II. Transition Plans

Federated strongly disagrees with the proposed requirements for transition plans.

1. **The proposed requirement for transition planning is highly unrealistic and would pose a daunting and burdensome new obligation for advisers.**

As with the proposed requirements for BC plans, the Commission justifies the proposed requirements for transition plans by reference to the need to protect investors from fraud and deception.[8] The Release then proceeds to outline an extraordinary body of planning, procedural, administrative and other requirements that must respond to both normal and hypothetical stressed market conditions.

> We believe that a plan of transition generally should account for transitions in both normal and stressed market conditions, and generally should consider each type of advisory client, the adviser's contractual obligations to clients, counterparties, and service providers, and the relevant regulatory regimes under which the adviser operates. Under the proposed rule, the transition components of a business continuity and transition plan ***would have to include*** (i) policies and procedures intended to safeguard, transfer and/or

[8] *Id.* at 43,536 ("Proper planning and preparation for possible distress and other significant disruptions in an adviser's operations is essential so that, if an entity has to exit the market, it can do so in an orderly manner, with minimal or no impact on its clients. As discussed above, an adviser's fiduciary duty obligates it to take steps to protect client interests from being placed at risk as a result of the adviser's inability to provide advisory services and, thus, it would be fraudulent and deceptive for an adviser to hold itself out as providing advisory services unless it has taken such steps. Such advance planning and preparation may minimize an adviser's exposure to operational and other risks and, therefore, lessen the possibility of a significant disruption in its operations, and also may lessen any potential impact on the broader financial markets. Accordingly, and as discussed in more detail below, we believe that SEC-registered advisers should be required to adopt and implement a written business continuity and transition plan that is tailored to the risks associated with the adviser's operations and includes certain components, reflecting its critical role as an agent for its clients.").

> distribute client assets during transition; (ii) policies and procedures facilitating the prompt generation of any client-specific information necessary to transition each client account; (iii) information regarding the corporate governance structure of the adviser; (iv) the identification of any material financial resources available to the adviser; and (v) an assessment of the applicable law and contractual obligations governing the adviser and its clients, including pooled investment vehicles, implicated by the adviser's transition. Each of the proposed required components of an adviser's transition plan is designed to help an adviser be well prepared for a transition so that it can act quickly and in its clients' best interests if and when a transition occurs. [9]

Remarkably, the Release appears to suggest that these requirements are modest and that the Commission might alternatively consider the more demanding "Living Wills" similar to what federal banking authorities require for the largest banks that are deemed to be systemically important financial institutions ("SIFIs").

> Should we adopt a more prescriptive rule that calls for a more specific transition plan similar to the "Living Wills" required by the Federal Reserve Board and the FDIC for large banks and systemically important non-bank entities? If so why, and what specifically should the rule require?[10]

It would be highly impractical and unduly expensive for advisers to comply with the proposed requirement. The circumstances around the need to transition assets are highly fact dependent. For example, servicing requirements, notice requirements, transfer restrictions and other terms and obligations under advisory contracts vary by product type, client and distribution channel. Systems used by advisers and client custodians also differ, raising compatibility issues. The circumstances around the need to transition assets in a stressed market environment are therefore highly speculative and far more difficult to address than for banks. Banks engaging in principal activities can subject their results to standardized stress tests and envision the potential need to liquidate assets in the context of a bankruptcy caused by a market or credit outcome. By contrast, advisers serve as agents for their clients and such macro events do not generally correlate with transition events for the great majority of advisers.[11] Therefore, the specific circumstances giving content to the proposed transition plans cannot be anticipated with a meaningful degree of certainty for the great majority of advisers serving investment companies, separately managed accounts or other clients. The proposed requirement therefore amounts to a detailed encyclopedia that is costly to produce and maintain, and whose primary benefit is not to inform the adviser, as there is no evidence that the absence of such plans has led to any material adverse effects on investors. The primary benefit appears to be for regulators who may be anxious that they do not understand the business decision-making process of the advisers they oversee, or who believe that living wills are now a form of regulatory best practice.

2. The need for such detailed transition plans as outlined in the Proposed Rule has not been demonstrated and is not justified on a cost/benefit basis.

The Release cites the 2008 financial crisis as demonstration of the need to protect investors from the risk of financial service firms unexpectedly exiting the market, and in footnote

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9 *Id.* at 43,542 (emphasis added).

10 Adopting Release, Adviser Business Continuity and Transition Plans, Exchange Act Release No. IA-4439, 48–49 (2016).

11 Certain hedge funds are an exception to this observation as they are more susceptible to macro events.

38 specifically cites Countrywide, Bear Stearns, Lehman Brothers, Fannie Mae, Freddie Mac, Merrill Lynch, Goldman Sachs, Morgan Stanley, AIG and Wachovia as examples of firms that were acquired or struggled over that period.[12] None of these firms are predominantly asset managers or were forced to exit the market because of their asset management affiliates. The industry has provided extensive comment that asset management poses starkly different risks than the principal activities of banks and broker-dealers.[13] The mere fact that some banks experienced solvency risks during the financial crisis cannot be bootstrapped to a conclusion for asset managers.

Furthermore, after considering the alleged systemic risk in the asset management industry, global financial regulators have determined that no asset managers pose systemic risks that warrant a SIFI designation, but that certain activities of asset managers, particularly relating to asset liquidity in open end vehicles, may warrant additional attention.[14] The Commission has separately identified such risks, which are the subject of additional rulemaking, such as the Commission's proposed rule on Liquidity.[15] Moreover, the Commission has announced that it intends to propose an additional rule on Stress Testing, pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act. It would be impossible for an adviser to meaningfully understand or comment on the elements of a proposed rule on transition planning in the absence of greater clarification on its obligations under these and other forthcoming rules. Similarly, it is premature for the Commission to justify the need for rulemaking on transition planning until it finalizes and assesses any gaps in industry practice that are exposed by these rules.

Within the asset management industry itself, there is a demonstration of remarkable stability reinforcing the conclusion that burdensome transition plan requirements are not warranted.[16] Although individual fund vehicles or advisers have occasionally closed (and

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12 Adviser Business Continuity and Transition Plans, *supra* note 1, at 43,535.

13 *See*, *e.g.*, Comment Letter of Fidelity Investments to Financial Stability Oversight Council's Notice Seeking Comment on Asset Management Products and Activities ("FSOC Notice") (Mar. 25, 2015), *available at* http://www.regulations.gov/document?D=FSOC-2014-0001-0022; Comment Letter of BlackRock, Inc. to FSOC Notice (Mar. 25, 2015) ("BlackRock FSOC Comment Letter"), *available at* http://www.regulations.gov/document?D=FSOC-2014-0001-0034; Comment Letter of Investment Company Institute to FSOC Notice (Mar. 25, 2015), *available at* http://www.regulations.gov/document?D=FSOC-2014-0001-0056.

14 *See* Financial Stability Board, Press Release Ref. no: 47/2015, Next Steps on the Assessment Methodologies for Non-Bank Non-Insurer Global Systemically Important Financial Institutions (NBNI G-SIFIs) (Jul. 30, 2015), *available at* http://www.fsb.org/wp-content/uploads/NBNI-G-SIFI-Next-Steps-Press-Release.pdf; International Organization of Securities Commissions, Securities Markets Risk Outlook 2016 (Mar. 2016), *available at* https://www.iosco.org/library/pubdocs/pdf/IOSCOPD527.pdf.

15 Commission, Release Nos. 33-9922; IC-31835, Open-End Fund Liquidity Risk Management Programs; Swing Pricing; Re-Opening of Comment Period for Investment Company Reporting Modernization Release 44–45 (2015), *available at* https://www.sec.gov/rules/proposed/2015/33-9922.pdf.

16 *See, e.g.*, Comment Letter of BlackRock FSOC (noting that "[t]ransitioning the management of client assets from one manager to another regularly occurs in the normal course of business" and listing 19 previous examples of advisers or funds exiting the market without great market impact); Comment Letter of Securities Industry and Financial Markets Association and the Investment Adviser Association to FSOC Notice (Mar. 25, 2015) (noting that "managers and funds routinely enter and exit the asset management industry" and citing an Investment Company Institute paper to note that, in 2013, "48 mutual fund sponsors left the business without any impact or distress"), *available at* http://www.regulations.gov/document?D=FSOC-2014-0001-0019; Comment Letter of PIMCO to FSOC Notice (Mar. 25, 2015), *available at* http://www.regulations.gov/docu

without material adverse impact), there has been no instance of a large adviser to registered funds or institutional separate accounts rapidly exiting the market. The Release itself describes in detail why transitions have historically had little adverse consequence for investors.[17] The rare occurrences we have observed do not substantiate an overarching requirement for all advisers to prepare and maintain the transition plans as required by the Proposed Rule.[18] Therefore, while the greatest regulatory concern presumably pertains to circumstances when large numbers of investors could be affected by a single adviser exiting the market, it is precisely such advisers for which the requirements of the Proposed Rule are patently unjustified on a cost/benefit basis. Federal courts have repeatedly upheld the requirement for cost/benefit justification and the recent MetLife decision makes it highly likely that regulatory actions based largely on theoretical concerns will be challenged and ultimately struck down.

3. **The need for baseline information on adviser transition planning can be satisfied by simpler and less costly means.**

If, notwithstanding the above comments, the Commission were to determine that some information on transition planning for asset managers could be informative within its oversight role, those objectives can be satisfied using far simpler and less costly means. The Commission could provide guidance under rule 206(4)-7 that would require advisers to assess the potential disposition of their business activities in certain environments, and maintain certain information that would be helpful to examiners in determining that the adviser has met this obligation. Such a framework could be captured in a principles-based assessment of what approaches the adviser would likely consider under a normal or stressed market circumstance. This analysis and planning would be separate and distinct from specific BC plans and would be addressed with

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ment?D=FSOC-2014-0001-0020; Comment Letter of Vanguard to FSOC Notice (Mar. 25, 2015), *available at* http://www.regulations.gov/document?D=FSOC-2014-0001-0055.

17 Adviser Business Continuity and Transition Plans, *supra* note 1, at 43,535 ("In the normal course of business, it is our understanding that advisers routinely transition client accounts without a significant impact to themselves, their clients, or the financial markets. We believe that much of this is largely attributable to the agency relationship of advisers managing the assets on behalf of their clients and the regulatory framework supporting this relationship whereby advisory client assets for which the adviser has custody are required to be held at a qualified custodian, such as a bank or broker-dealer. Because client assets custodied by an adviser must be held at a qualified custodian and segregated from the adviser's assets, we have observed that transitioning accounts from one adviser to another can largely be a streamlined process that in many cases may not involve the physical movement or sale of assets. Pooled investment vehicle clients generally have the ability to terminate the advisory contract of the adviser or remove the governing body that may provide advisory services (*e.g.*, general partner or managing member) and appoint a new adviser or governing body if they so desire, while separate account clients can generally terminate the advisory contract and appoint a new adviser to manage their assets, all while their assets are typically maintained at a qualified custodian.") The Release also identifies situations of "non-routine" disruptions leading to transitions that did not have "a significant adverse impact on clients, fund investors, or the financial markets," citing the spin-out of Neuberger Berman from Lehman Brothers during the 2008 financial crisis. *Id.* at 43,535–36.

18 *Id.* at 43,536 ("We are also aware of transitions involving funds under stress that have not been seamless or without problem."). The Release then cites just four occurrences of such transitions involving F-Squared Investments, Inc., Strong Capital Management, Inc., Primary Reserve Fund, and Long Term Capital Management, LLP. *Id.* at 43,536 n.36; *see* Comment Letter of Investment Company Institute to Proposed Rule at A-1 (Aug. 23, 2016), https://www.sec.gov/comments/s7-13-16/s71316-6.pdf (discussing these transitions and their limited relevance as a basis for the Proposed Rule on transition planning).

separate guidance. In particular, although BC plans and transition plans share the concept of planning for future contingencies regarding the adviser's business activities, they are radically different in content. BC plans are largely tactical and operational in nature whereas transition plans are primarily strategic and financial, but with operational considerations. They are performed by different individuals within the firm and generally describe activities over very different time periods. Because actual future transitions depend heavily on the events giving rise to the transactions, among other facts and circumstances, transition plans cannot be granular or detailed, especially in stressed conditions when, by definition, the events are unfolding quite outside the advisers' regular business plans. For these reasons, transition plans are an entirely separate exercise than BC plans, and the two should not be confused or encapsulated within the same rule or guidance.

III. Responses to Specific Questions Posed in the Release

Enclosed are Federated responses to questions posed in the Release.[19]

- ***Should we require all SEC-registered advisers to adopt and implement business continuity and transition plans? Or should we identify only a subset of SEC-registered advisers that must implement such plans? Which advisers should be in such a subset (e.g., large advisers with assets under management over a specific threshold, advisers affiliated with financial institutions, etc.) and why?***

  The Commission's argument for requiring BC plans is that it would be fraudulent and deceptive for an adviser to hold itself out as a fiduciary and not have effective BC plans that address the concerns raised by the Commission. Because every investor is entitled to protection from fraud and deception, the Commission must therefore require BC plans for all advisers if this argument is to be relied on as the basis for rulemaking. The first principles of cost/benefit analysis, however, make it clear that advisers must be permitted to calibrate their BC plans to the nature, size and scope of their advisory services. Furthermore, a significant defect of the proposal is the omission of any role for BC risk disclosure. Advisers should be required to disclose the existence of their BC plans and their general nature, as well as the risks associated with events that cannot be foreseen or economically prevented.

- ***Rather than adopting the proposed rule, should the Commission issue guidance under rule 206(4)-7 under the Advisers Act addressing business continuity and transition plans? If so, should that guidance set forth possible elements of such a plan?***

  Federated strongly recommends that the Commission not issue a specific rule on BC or transitions plans, but instead rely on guidance under rule 206(4)-7. The industry is in a state of rapid evolution and the role that regulators must play in overseeing market utilities is still developing. It is therefore premature to issue a specific rule on BC or transition plans in the form proposed.

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19 Adopting Release, *supra* note 10, at 46–52.

While the Proposed Rule covers the diverse BC risks, the areas of greatest focus relate to cyber risk and the performance of critical vendors such as custodians, transfer agents or trade execution platforms. Recent events demonstrate that the largest and most sophisticated financial firms that invest enormous sums in information security remain exposed to hacking threats. Therefore, the mere occurrence of a cyber event is not indicative a failure to have policies reasonably designed to prevent harm. Conversely, even the largest service providers to the asset management industry generally do not provide the transparency regarding their own BC plans or information security programs sufficient to enable advisers to have confidence that those firms are in compliance with the Release; or that the adviser's reasonably designed BC plans could rely on the statements made by such firms. Prior to promulgating a new rule on BC, the Commission should work with the industry and service providers to develop the appropriate form of attestations (such as SOC 2s) that advisers could then employ in crafting their own compliance programs. In the absence of such standards, an adviser could face a liability in the event that it did not effectively in-source via a BC plan the functionality that is thought to be outsourced to the large vendors. This would create an unreasonable burden that does not meet a cost/benefit justification.

Similarly, the Release creates the unreasonable expectation that all cyber or vendor contingencies can be anticipated and defended against. In fact there is a risk of significant cyber or natural events that prevent the use of critical infrastructure or vendors. In these cases, no adviser could reasonably be expected to have in place back-up systems to completely eliminate potential adverse impacts on investors. Advisers should be afforded safe harbor protections against such contingencies and disclosure alerting investors to these risks should be mandated.

- ***What, if any, implications will the proposed rule have for investment advisers that are also subject to other regulatory requirements as to business continuity and/or transition planning (*****e.g.,** ***FINRA or CFTC rules on BCPs)? For example, would the proposed rule be inconsistent with an advisers obligations under other regulatory requirements?***

  Investment advisers should not be subject to conflicting or duplicative regulation. The Commission should work with other regulators to develop a unified approach or determine that, when there are inconsistencies, compliance with the Commission's regime will be deemed to satisfy the requirements of other regulators.

- ***Should we require business continuity and transition plans to include each of the proposed components? Alternatively, should the rule require advisers to have a business continuity and transition plan, and specify certain components of a plan in the form of a safe harbor provision? Or, should the rule not specify required components of a plan and instead allow advisers to determine the appropriate components of their plans? Are there any components we should remove from the proposed list of required components? Are there any components we should add or expand upon? For example, with respect to a pre-arranged alternate physical***

location(s) of the adviser's office(s) and/or employees, should we require that an adviser's business continuity and transition plan include an alternate location at a specified distance away from its primary location? Should we require an adviser's communication plan to extend to investors in certain types of pooled investment vehicles? If so, which specific types of pooled investment vehicles and how should the term "investors" be defined for each type of pooled investment vehicle? Should we require an adviser to have policies and procedures that address the identification, assessment, and review of critical third-party vendors that the adviser arranges or oversees for its clients?

Federated believes that it is reasonable for Commission guidance or any future rule to set forth categories or components of BC and transition plans that advisers should consider, to the extent applicable to the adviser. This will assist in clarifying expectations and establishing a common framework for all advisers. The extent of detail in any particular plan should depend on the particular circumstances of that adviser and the issues being addressed. If the Commission elects to set forth possible elements of BC or transition plans, either in the form of guidance or a final rule, it should clarify that advisers may reasonably determine that certain of the recommended elements are not applicable to its operations, and the omission of such elements from an adviser's plans would be appropriate and consistent with such guidance or rule.

- ***Are there any components of the NASAA model rule or guidance, or other rules or guidance addressing BCPs, that we have not addressed in the proposed rule that we should address? Should advisers with certain types of clients, including for example advisers to registered investment companies or sponsors of wrap programs, be required to undergo additional obligations with regard to adopting and implementing a business continuity and transition plan? What additional steps should such advisers be required to take with respect to such clients and/or such clients' service providers?***

  The Commission's statutory mandate to promote efficiency, competition and capital formation has led to great diversity across the industry in both adviser size and configuration and in the types of investment vehicles they oversee. The BC requirements of a large money market fund offering daily liquidity to investors is quite different from that of a long-only equity hedge fund with quarterly withdrawals. Consequently, specific BC plans should be tailored to the specific attributes of the adviser and its clients. The overall guidance provided by the Commission, however, should reflect the general principles guiding all BC plans.

- ***Are each of the proposed components of a business continuity and transition plan clear or should we provide additional information and/or definitions for any of the components? If so, what additional information or definitions are needed? For example, should we provide a definition of "significant business disruption," "unable to continue providing investment advisory services," or "pooled investment vehicle"? Alternatively, should we require investment advisers to define certain terms, like***

"significant business disruption" or "unable to continue providing investment advisory services," within their plans?

The industry is not served by vaguely defined terms or unrealistic expectations. In some sections the Release refers to policies and procedures that are "reasonably designed" to meet the objectives of the Proposed Rule. In other sections, the Release implies that BC risks must be "minimized." An adviser can only create BC plans relating to events that can be "reasonably anticipated." Even then, many events that could be anticipated, such as the complete loss of critical infrastructure, cannot be realistically mitigated by an adviser's BC plan. Instead, the wording of the Release could be construed to imply extraordinary regulatory or civil liability for ***any*** BC event that was not anticipated by the adviser's planning exercises. Such a vaguely defined standard could be interpreted to require extraordinary investments by advisers to defend against risk scenarios that are impossible to predict. Such a standard would fail to meet a cost/benefit challenge and would thwart competition in the industry by raising barriers to entry.

- ***Should all advisers be required to include each of the proposed components in a business continuity and transition plan or should certain advisers be exempt from including certain components? If certain advisers should be exempt, why? For example, should only certain advisers be required to adopt and implement the transition plan component of the proposed rule or is there a subset of investment advisers with operations so limited that the adoption and implementation of a transition plan (or certain components of the transition plan requirement) would not be beneficial? If so, what criteria could be used to identify this subset of advisers? Are there alternative or streamlined measures that these advisers could take to facilitate an orderly transition in the event of a significant disruption to the adviser's operations? If these advisers did not have transition plans, should they be required to disclose the absence of such plan?***

  See above. Federated strongly believes that transition plans should not and cannot be detailed execution plans because the specifics of the transition activity will depend heavily on the facts and circumstances causing the transition. Therefore, transition plans should be higher level principles-based assessment of what transition activity may be appropriate in differing environments. Such plans must naturally be tailored to the specific circumstances, size, configuration, asset mandates and other characteristics of the adviser.

- ***With respect to each of the proposed components of a business continuity and transition plan, we have provided information as to the items and/or actions that we believe generally should be encompassed within a particular component. Is there additional information that we should provide, or any information that we should exclude or modify, regarding any of the proposed components of a plan? Alternatively, instead of permitting advisers the flexibility to draft their plans based on the complexity of their businesses, should we require advisers to address each component in a prescriptive manner by requiring specific mechanisms for addressing particular risks?***

Federated believes that the Commission should identify the broad principles and categories of risk against which it believes clients should be protected; and in crafting their BC plans each adviser should be given the discretion to determine which of them apply to the business of that adviser. The examination process should identify whether a given adviser has met the requirements of the guidance.

- ***Should we adopt a more prescriptive rule that calls for a more specific transition plan similar to the "Living Wills" required by the Federal Reserve Board and the FDIC for large banks and systemically important non-bank entities? (These resolution plans require, among other things: (a) information regarding the manner and extent to which any insured depository institution affiliated with the company is adequately protected from risks arising from the activities of any nonbank subsidiaries of the company; (b) full descriptions of the ownership structure, assets, liabilities, and contractual obligations of the company; and (c) identification of the cross-guarantees tied to different securities , identification of the major counterparties, and a process for determining to whom the collateral of the company is pledged. See Resolution Plans, supra note 40.) If so why, and what specifically should the rule require?***

Federated strongly disagrees with the Release's proposed requirements for transition plans. Unlike banks, investment advisers do not take principal risks with the assets under management and therefore do not have the equity volatility or systemic risk of banks. No investment managers have been designated as SIFIs. There have been very few occasions when investment advisers of mutual funds have become insolvent or been forced to close down. There is no cost/benefit justification for the Commission to require detailed and costly transition plans that prescribe the resolution of an investment adviser under the proposed "normal or stress market conditions." Furthermore, since these instances are so rare, and the circumstances under which they would occur are so difficult to predict, it is impossible to state a detailed or granular plan according to which some portfolio, fund or line of business would be transitioned to another manager in a normal or stressed environment. Such transitions typically occur over months with detailed negotiations that consider every aspect of the transaction.

For these reasons, Federated believes that the proposed requirement for transition plans should be treated separately from the requirements for BC plans. For the reasons stated, the transition plan requirement itself cannot realistically be a detailed playbook as is the case with some BC plans. The facts and circumstances, and the great unknowns, around large-scale business events only permit that transition plans be stated as a principles-based outline of the general approach to differing lines of business.

- ***As part of the proposed rule, should we require advisers to provide disclosure to their clients about their business continuity and transition plans? If so, what should be the format of such disclosure (*****e.g.,*** ***summary of plan, copy of plan)? When or how frequently should this disclosure be provided? Should we require advisers to disclose to their clients incidents where they relied on or activated their business continuity and***

transition plans? If so, what should be the format of such disclosure? What types of incidents should be disclosed or not disclosed?

Federated strongly believes that it is inappropriate for advisers to disclose the details of their BC plans or transition plans to clients or the public. Such plans contain proprietary information that could be damaging to the adviser and the adviser's clients if made public. It is appropriate for advisers to disclose the existence of such plans, the general nature of the plans, and the possible existence of continuity or transition risks that cannot be economically prevented or foreseen. Advisers should be given safe harbor protections against extraordinary cyber or BC events that cannot be anticipated or economically prevented.

- ***As part of the proposed rule, should we require advisers to report to the Commission incidents where they rely on their business continuity and transition plans? If so, under what circumstances should advisers be required to report to the Commission and how should advisers report this information? When should the required reporting occur?***

  Federated believes that it is reasonable to require that advisers timely report to the Commission any events that materially disrupt operations as a result of which the adviser relied on a BC plan or transition plan. Such communication may vary in form depending on circumstances, but in most cases verbal alerts to appropriate Commission personnel should suffice.

- ***Should we require advisers to file their business continuity and transition plans, or a summary thereof, with the Commission? Should these filings be made available to the public? Why or why not? Are business continuity and transition plans considered proprietary to an adviser such that disclosing its plan to the public (either through a Commission filing or through disclosure to a client) creates additional risk exposure to the adviser?***

  Federated strongly opposes disclosing BC plans or transition plans to the public. These plans contain proprietary and confidential information that could be damaging to advisers and their clients if made public. Federated believes that BC plans and transition plans should be available to the Commission during periodic examinations, but should not be filed with the Commission, as is the case with most other compliance requirements. BC plans can be voluminous with frequent updates and it would be an administrative burden without cost/benefit justification to maintain such detailed records with the Commission.

- ***Should we require that business continuity and transition plans be reviewed at least annually, as proposed? Should we expressly require reviews of business continuity and transition plans to be documented in writing? Should we require more frequent or less frequent review of business continuity and transition plans? In addition to annual review, should we require that advisers review their plans when specific events occur? For example, should we require plans be reviewed when an adviser has an event that***

causes it to rely on its plan? Should we require plans be reviewed based on changes to the adviser's operations or processes, changes in the ownership or business structure of the adviser, compliance or audit recommendations, lessons learned from testing or disruption events, and/or regulatory developments?

Investment advisers are in the business of managing client assets. Yet the Commission does not prescribe how often portfolios must be reviewed, or what the reviews consist of, or that they be documented in writing, etc. Similarly, continuity planning is now part of the fabric of the adviser's business activity. It is reasonable to require that BC plans be reviewed annually, but the suggested maintenance of reviews, or the obligation to review or update them based on particular events, imposes arbitrary requirements that may often have no relationship whatsoever to the protection of an adviser's clients in practice. Federated proposes principles-based guidance that advisers interpret in the context of their business, which is then examined for adequacy during period Commission exams.

- ***Should we require advisers to report to the Commission regarding the annual review of their business continuity and transition plans? If so, what should be the format of the report?***

  Federated proposes that advisers annually report to applicable boards of directors of registered funds, and to other clients requesting such reports, the process and substance of BC plan reviews, and that the books and records pertaining to such reviews be maintained for Commission examination purposes.

- ***Should we explicitly require advisers to annually review the business continuity and transition plans of their third-party service providers that provide critical services to the adviser and its clients? If so, how should these reviews be conducted? What types of documentation could be requested to perform these reviews?***

  See above. Federated strongly believes that service providers to investment advisers must be required to maintain rigorous BC plans that are consistent with the requirements placed on advisers. Without jeopardizing the confidential information of the vendor in a manner to place it at undue cyber or business risk, such plans, or appropriate attestations regarding these plans, should be made available to advisers so that they may conduct the appropriate diligence on critical service providers.

- ***Should we specifically require advisers to periodically test their business continuity and transition plans or certain material components thereof to assess whether the plans are adequate and effective? If so, how should such testing be conducted? What should be included in the scope of such review? How often should such testing be required?***

  Periodically testing BC plans is a principle that should be outlined in the guidance. How best to implement testing should be left to the discretion of the adviser based on the circumstances of the adviser's business. The adviser should report to applicable fund boards and to other clients requesting such reports compliance with the principles identified in the guidance.

- ***Should we require advisers to maintain copies of their business continuity and transition plans that are in effect or were in effect at any time during the last five years, as proposed? If not, what, if any, recordkeeping requirements should we adopt with respect to business continuity and transition plans? Is five years an appropriate retention period? Should it be longer or shorter? Why?***

Federated recommends that BC plans and major updates thereto be maintained for a period of five years. Plans are often in some state of adjustment, however, and it is unwieldy to maintain every version of every plan for five years. Federated recommends maintaining annual snapshots of BC plans for record retention purposes.

- ***Should we require advisers to keep any records documenting their annual review of their business continuity and transition plans, as proposed?***

Federated recommends that advisers simply record the changes in the plans themselves and not the annual review of each plan. We propose that the adviser review with the applicable fund boards and other clients requesting such reviews the plan update process.

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Federated hopes that the Commission finds these comments helpful and constructive and is happy to provide additional information relating to our comments or discuss any questions you may have.

Yours very truly,

Michael R. Granito

Senior Vice President

Chief Risk Officer

cc: The Honorable Mary Jo White
The Honorable Kara M. Stein
The Honorable Michael S. Piwowar