August 16, 2022

Ms. Vanessa A. Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

Re: Request for Comment on Certain Information Providers Acting as Investment Advisers [Release No. IA-6050; File No. S7-18-22; 87 FR 37254]

Dear Ms. Countryman:

The Index Industry Association (IIA or we) appreciates the opportunity to share our views on the U.S. Securities and Exchange Commission's (Commission) request for comment on "Certain Information Providers Acting as Investment Advisers" (Comment Request), which seeks input on various questions to assist the Commission in determining whether the actions of certain information providers, including index providers, meet the definition of "investment adviser" under the Investment Advisers Act of 1940 (Advisers Act) or the Investment Company Act of 1940 (Investment Company Act).

The IIA was founded in 2012 as a not-for-profit organization composed of independent index providers from around the world. Many of the leading independent index providers are members of the IIA, including Bloomberg Index Services Limited, Cboe Global Indices, the Center for Research in Security Prices, China Central Depository and Clearing (China Bond Pricing), China Securities Index Co. Ltd., FTSE Russell, Hang Seng Indices, ICE Data Indices, JPXI (Tokyo Stock Exchange), Morningstar, MSCI Inc., Nasdaq OMX, Parameta Solutions, Shenzhen Securities Information Co Ltd., S&P Dow Jones Indices and STOXX Qontigo.

The IIA's mandate is to educate investors on the attributes and role of indices within the investment process; to advocate for the interests of both index users and providers worldwide; and to work with regulators and other representative bodies to promote competition and push for industry standards of best practice, independence and transparency. As independent index providers, IIA's members do not trade the underlying component securities in their indices or issue investable financial products that track or use indices.[1] As explained in further detail below, this independence model prevents the real and perceived conflicts of interest that may arise in certain index providers that do not separate such business functions.

[1] We note that some IIA members are affiliated with exchanges which may be trading venues for an index's underlying component securities or for index-linked investment products, or to which indices are licensed for use in the development of derivative investment products.

Though the IIA appreciates, and shares, the Commission's desire to protect investors, the IIA opposes the Commission's novel suggestion in its Comment Request to regulate index providers as investment advisers under the Advisers Act or the Investment Company Act. We respectfully submit that such an outcome would directly contradict federal securities laws and rules, as well as established market practices; dramatically increase costs for U.S. investors with no benefit in return; result in widespread confusion among market participants and investors about their respective roles and obligations; and undermine the strong measures that index providers have undertaken to provide well-functioning, independent indices that support the strength of U.S. capital markets. Further, the Commission's suggestion to regulate index providers as investment advisers would impose a regulatory framework and fiduciary duty to act in the best interests of each of its clients that fundamentally conflicts with the role and obligations of global index providers to administer indices in an independent, transparent manner without conflicting obligations under the International Organization of Securities Commissions' (IOSCO) Principles for Financial Benchmarks (IOSCO Principles), the Benchmarks Regulation in the U.K., the Benchmarks Regulation in the EU, and other similar existing regulation of index providers globally.[2]

The term "index" is not defined in the Comment Request or in the federal securities laws generally. The IIA's official definition of an index is "a number calculated by reference to a theoretical collection of assets, market indicators, securities or derivatives whose absolute level or periodic difference relate to the performance of the theoretical collection over that period." In less technical terms, an index measures the performance, or some other characteristic, of a list of instruments (*e.g.*, bonds, stocks, commodities, derivatives) that are selected and weighted according to an employed methodology that describes a set of rules governing the construction of the index. The purpose of an index is to represent a market segment (*e.g.*, large or small cap U.S. or global equities), asset class (*e.g.*, equity or fixed income), industry sector (*e.g.*, health care or energy), investment factor (*e.g.*, growth/value, volatility, or dividends), or other investment strategy or theme (*e.g.*, target date). Indices are designed to measure specified markets objectively so that users of market information, particularly investors and their advisers, can make informed decisions that align with their goals. If indices were created or maintained as the index provider or another actor wished, as opposed to in accordance with specified rules and methodologies, an index may present inaccurate or inconsistent information, which would ultimately undermine investors' ability to make informed decisions, as well as the index's, and the index provider's, market credibility. Thus, when constructing or rebalancing an index, the index provider does not make any judgment as to the merit of an investment in the index components. Rather, it is a mechanical process where all of the securities that satisfy the pre-established rules for the index are included, regardless of their investment merits.

Section 202(a)(11) of the Advisers Act defines an investment adviser as any person who: (1) provides advice about securities (2) for compensation (3) to others.[3] To be an investment adviser

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[2] *See, e.g.*, the benchmark regulations of South Korea, Japan, Singapore and Australia. Additionally, India and South Africa are currently considering proposed benchmark regulations.

[3] Under Section 202(a)(11) of the Advisers Act, an "investment adviser" is: "any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of

under this provision, an entity must satisfy all three factors. Although the meaning of being engaged in the business of providing advisory services to others is not entirely clear on the face of the Advisers Act, the Commission has provided interpretive guidance applicable to certain service providers. For example, in determining the investment adviser status of persons who provide financial services such as financial planning or pension consulting services, the Commission has stated that such a person is engaged in the business of providing investment advice if it: (1) holds itself out to the public as an investment adviser or as one who provides investment advice; (2) receives any separate or additional compensation that represents a clearly definable charge for providing advice about securities; or (3) provides specific investment advice other than rarely or in isolated or non-periodic instances.[4] Commission staff has stated that a person may be viewed as holding itself out as an investment adviser if it: (1) advertises itself as an "investment adviser;" (2) refers to itself as an "investment adviser;" (3) maintains a listing as an investment adviser in any telephone, business, building, or other directory; (4) uses letterhead, stationery, or business cards indicating any investment advisory activity; or (5) otherwise lets it be known, through word of mouth or other means, that it is willing to provide investment advisory services.[5]

As a general rule, index providers have taken the stance that they do not meet the definition of an "investment adviser" under the Advisers Act and, accordingly, index providers are not required to register as an investment adviser with the Commission. Index providers typically provide services related to (1) conceptualizing the rules that will determine the components of the index and how the index will be maintained, (2) calculating the index values in accordance with the rules established for the index, and (3) publishing or otherwise disseminating the values of the index. Index providers also frequently license the use of their intellectual property related to the index to fund managers, sponsors of investment products and other types of entities for a variety of uses.[6] In performing these functions, the index provider does not provide advice about securities. Specifically, the index provider does not provide any opinion or view as to whether it would be advisable for any investor to purchase or sell the securities that are components of the index. Rather, the index provider simply administers the index as a category of securities or other grouping of instruments that represents a particular segment of the market. Further, index providers do not hold themselves out to the public as an investment adviser or as one who provides investment advice, do not receive any separate or additional compensation that represents a clearly definable charge for providing advice about securities, or provide specific investment advice. In fact, index providers typically disclaim any investment advisory responsibility in connection with publishing and licensing its indices. Index providers do not manage assets or report "assets under

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securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities."

[4] *See* Applicability of Investment Advisers Act to Financial Planners, Pension Consultants, and Other Persons Who Provide Investment Advisory Services as a Component of Other Financial Services, Investment Advisers Act Release No. 1092 (Oct. 8, 1987), available at https://www.sec.gov/rules/interp/1987/ia-1092.pdf.

[5] *See* Applicability of Advisers Act to Financial Advisors of Municipal Securities Issuers, Staff Legal Bulletin No. 11 (Sept. 19, 2000), available at https://www.sec.gov/interps/legal/slbim11.htm.

[6] Please see our response to Question 3, *infra*, for more information.

management." Additionally, they do not recommend or advise on asset allocations, investment products or investment strategies.[7]

Certain index providers create custom indices according to specific clients' needs. For example, active fund managers with widely diversified portfolios found that comparisons to even an extremely broad equity index or fixed-income index may be misleading to investors because the performance characteristics of the various asset classes in their portfolio may have been purposefully selected so that they do not correlate with each other, or due to the fact that the broad index may violate one or more of their investment policy guidelines (*e.g.*, limits on individual exposures). To address this growing market need, index providers began to produce custom indices, such as by blending together existing indices from two or more asset classes or by imposing exposure caps, that could more accurately measure the performance of certain actively managed portfolios. Some index providers provide direct indexing services, which involve wealth managers and investment advisers selecting indices for their clients that they determine are suitable for their individual clients' investment needs.

At no stage of the creation, maintenance or licensing of a custom index does the index provider provide any form of personalized advice or recommendation to the investment adviser or the investment company, or their clients. Further, in no event does the index provider, in connection with any custom index or direct indexing, have any assets under management or issue investable financial products. The index provider typically provides written notices to the licensees of a custom index clearly stating its limited role, including that it does not provide any investment advice. In fact, many index providers require the licensees of custom indices to provide these notices to their clients.

The Commission's suggestion that index providers be regulated as investment advisers represents a dramatic departure from the longstanding, industry-accepted position that the creation, maintenance or licensing of indices does not constitute investment advice.[8] This is of particular concern since the Comment Request did not raise any issues regarding current index provider business practices or behaviors that would warrant such a major policy reversal. Even Professors Paul Mahoney and Adriana Robertson, the academics on whom the Commission relies heavily in its Comment Request, admit that "potential for index providers to exercise their discretion in self-

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[7] *See supra* note 1.

[8] For example, we note that IOSCO's Task Force specifically consulted as to whether the IOSCO Principles should cover equity indices. *See* Principles for Financial Benchmarks Final Report, International Organization of Securities Commissions, at 30 (July 17, 2013).

After receiving broad support in the public comments, the Task Force determined that although the publicly traded securities prices underlying securities indices pose fewer regulatory concerns than other, less-objective submission data for commodities indices, a proportionate application of the IOSCO Principles to equity indices was beneficial. *See id.*

As far as the IIA is aware, no Task Force member, other regulator or any other person was recorded as having raised the issue of whether securities indices involve discretion and therefore should be regulated as investment advice.

interested ways…has not to date generated widespread abuses."[9] Instead the Professors query, "Why shouldn't the [Commission] refrain from acting unless and until abuses occur."[10] However, the question "why not?" should not be used to justify prioritizing a major rule change that would significantly, negatively impact an established, well-functioning ecosystem in the market.

The value and benefits that indices and indexing have brought to investors cannot be overstated. Indices help with financial awareness and literacy. For example, contemporary understanding of financial markets is driven almost entirely by an explicit or implicit use of indices. References to "the market" are almost always a reference to an equity stock market index that is used as a proxy measurement for the performance of a national economy (*e.g.*, S&P 500 or the Dow Jones for the U.S., the FTSE for the U.K.). They have also allowed for innovative index-based financial products that allow individual investors to obtain access to a diversified portfolio of investments at low cost and effort, such as index-based mutual funds and exchange-traded funds (ETFs). A 2021 S&P Dow Jones Indices' study estimated that indexing had generated approximately $357 billion in cumulative savings in management fees.[11] Indices have also been used to bring comparability (and, therefore, increased transparency and accountability) to the active fund management industry, by serving as benchmarks for performance results.

Should the Commission impose fiduciary obligations on index providers as investment advisers, the negative consequences on the use of indices would be immediate and drastic. For example, such designation would introduce friction into a well-functioning system by requiring index providers to take on fiduciary duties that they are not suited to discharge. Additionally, the designation would cause conflicts of interest to arise for index providers as, for any given index, they would now have to act on behalf of various advisory clients, each with differing investment goals, rather than as independent index providers. The designation would also bring about significant regulatory confusion, such as in regards to: (1) the treatment of advisory clients that, in turn, owe fiduciary duties to their own advisory clients; (2) the enforceability of index provider agreements, which typically state that index providers are not investment advisers and are not responsible for errors; (3) whether indexed ETFs, as unmanaged unit investment trusts, may continue to use the services of index providers who are investment advisers; and (4) the administration of globally available indices. The designation would also significantly increase compliance costs for index providers, which not only raises the financial barrier to entry but will subsequently cause consolidation and reduce competition in the index industry. Moreover, the surviving index providers and their licensees most likely will be forced to pass the increased costs on to investors.[12] The resulting chill that would befall the industry would severely hamper the numerous aforementioned benefits that have been brought about by indexing.

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[9] Paul G. Mahoney & Adriana Z. Robertson, *Advisers by Another Name*, University of Virginia School of Law, Law and Economics Paper Series 2021-01 (Jan. 2021).

[10] *Id.* at 5.

[11] Anu Ganti, *Strength of Savings*, Indexology Blog (July 27, 2021), available at https://www.indexologyblog.com/2021/07/27/strength-of-savings/.

[12] An increase of even a few basis points in fees could drive up costs for U.S. investors in indexed products by billions of dollars per year and enable fund managers to maintain their fees commensurately higher.

The IIA and its members recognize the importance of upholding high standards of integrity and transparency in our industry to promote sustainable global financial markets and foster healthy competition and innovation. Each IIA member commits to adhering to the IIA's Best Practice Guidelines (Guidelines), a set of standards regarding an index provider's governance arrangements and management structure; data collection processes; index calculation and verification methodologies; publication timing; management of its conflicts of interest; business continuity and disaster recovery plans; recordkeeping and confidentiality policies; complaints process; and internal controls.[13] Further, the Guidelines are available to non-member index providers. The Guidelines were developed by the IIA in July 2013 and are regularly maintained.

In addition to the Guidelines, many index providers adhere to the IOSCO Principles.[14] The IOSCO Principles, which the Commission helped draft, establish policy guidance and principles for index-related activities that address conflicts of interest and promote good index design and robust transparency. Some IIA members provide public statements of adherence with detailed descriptions of their control frameworks to funds, asset managers and other users of their indices, with internal or external auditors often conducting assessments of the controls described in these statements.

IIA has long been a vocal proponent of enhancing market transparency, fostering robust competition among market participants, and ensuring high quality market measurements that facilitate informed investor decision-making. However, requiring index providers to register as investment advisers does none of these things. Alternatively, IIA is generally supportive of initiatives that seek to incorporate review of index providers and their control frameworks into a fund's or investment adviser's compliance program. Having funds and investment advisers review an index provider's index governance, operations, business continuity plans, cyber security, business code of ethics and compliance framework is a sound alternative way to address the Commission's concern of protecting fund shareholders without imposing undue regulatory burdens and increased compliance costs on index providers. Investment advisers, in particular, are well-suited for this role, as they already play a key role in index provider selection and are familiar with index provider contract terms, associated fees and the process of monitoring index performance.

To ensure that such reviews do not become too burdensome for funds and investment advisers, the IIA urges the Commission to clarify that an internal or external audit report in adherence to IOSCO Principle 17 will satisfy such review requirement except in certain extenuating circumstances (*e.g.*, the fund or investment adviser becomes aware of a significant control failure that the fund or investment adviser believes warrants further investigation).

We have attached our detailed responses to the Comment Request's questions, including our analyses regarding why index providers are not investment advisers under the Investment Company Act and the applicability of the Publisher's Exclusion should the Commission determine that index providers are investment advisers under the Advisers Act. Thank you for your

[13] The Guidelines are available at https://www.indexindustry.org/iia-best-practice-guidelines/.

[14] The IOSCO Principles are available at https://www.iosco.org/library/pubdocs/pdf/IOSCOPD415.pdf.

consideration of these responses. We stand ready to discuss them further with Commission staff at your convenience.

Respectfully submitted,

Rick Redding
Chief Executive Officer
Index Industry Association

IIA Response to the Comment Request

Question 1:

Are our descriptions of each information provider accurate and comprehensive? What types of potential risks and conflicts of interest does each type of provider present? How many providers of each type do commenters estimate currently offer their services in the United States?

IIA Response to Question 1:

The IIA does not agree with the Commission's characterization of index providers in its Request for Comment, including with respect to the "significant discretion" they supposedly exercise.[15] The Commission's description erroneously implies that index providers have "significant" discretion in calculating and maintaining indices, including during index reconstitution (when changes, such as adding or dropping particular constituents, are made to an index) and index rebalancing (the process of modifying an index's weighting). This description is contrary to current, well-established industry practice.

Index providers aim to avoid the use of discretion by utilizing rules-based methodologies. However, administrative discretion in an index methodology is acceptable. Accordingly, index providers implement policies and procedures to develop and maintain indices pursuant to transparent methodologies that only permit a limited exercise of discretion within the confines of the applicable index methodology. Index methodologies may permit index providers to exercise such discretion only in accordance with methodological objectives and under limited circumstances (*e.g.*, market stress, market disruption, an atypical corporate action event). Please see our response to Question 11 for a more detailed explanation on the use of discretion when creating and maintaining custom indices specifically.

The many index providers who adhere to the IOSCO Principles commit to the following:

- Pursuant to IOSCO Principle 3, to adopt a conflicts of interest mitigation framework that should include measures to avoid, mitigate or disclose conflicts of interest that may exist between the index provider business and any other business of the index provider or its affiliates; to disclose conflicts of interest arising from the ownership structure or control of an index provider to stakeholders and relevant regulatory authorities in a timely manner; and to protect the integrity and independence of benchmark determinations;

[15] The Commission states in the Comment Request: "Index providers compile, create the methodology for, sponsor, administer, and/or license market indexes. They typically determine the particular 'market' (which may be a sector or other group of securities) that the index measures, the index constituents that measure that market, and the weightings that each constituent receives. Once the index is designed and its methodology is created, index providers determine the index's level (or measurement) pursuant to that methodology. These activities leave room for significant discretion—for example, an index provider typically has the ability to make changes to the index by adding or dropping particular constituents (i.e., index reconstitution) or modifying their weighting within the index (i.e., index rebalancing), in some cases without publicly disclosing their index methodologies or rules." Request for Comment on Certain Information Providers Acting as Investment Advisers, 87 Fed. Reg. 37,254 at 37,254-55 (June 22, 2022).

- Pursuant to IOSCO Principle 4, to implement, and periodically review and update, an appropriate control framework for the process of determining the index that addresses the extent of the use of discretion in the index setting process, as well as ensuring the integrity and quality of the index determination process through various robust accountability measures;

- Pursuant to IOSCO Principle 11, to document and publish, or make available, the methodology used to make an index, including the criteria and procedures used to develop the index, the mix of inputs used to derive the index, an explanation of how priority of certain data types is assigned, the minimum amount of data needed to determine the index, and the guidelines that control the exercise of any discretion used by the index provider[16]; and

- Pursuant to IOSCO Principle 12, to publish or make available the rationale of any proposed material change to an index methodology, as well as the procedures for instituting such change[17].

The Guidelines—which every IIA member commits to comply with as part of its membership, and which are available to other non-member index providers—impose similar requirements. For example, Standard 2 of the Guidelines (regarding the quality and transparency of index methodologies) requires that an index provider publish or otherwise make available the index methodologies for indices that are intended for commercial use. Standard 2 further provides that index providers should clearly document the methodology for each index intended for commercial use, to the extent practicable and allowed without violating any agreements or applicable laws restricting such publication. The published index methodology should include a description of the objective of the index and how the index is calculated and maintained. The description should be

[16] We note that IOSCO Principle 11 further requires the publication to include "the rationale for adopting the particular methodology, with sufficient detail to allow stakeholders to understand how the index is derived and assess its representativeness, its relevant to particular stakeholders and its appropriateness as a reference." Additionally, IOSCO Principle 11 requires that the index methodology publication further contain: (1) definitions of key terms; (2) procedures and practices designed to promote consistency when an index provider exercises any discretion or judgment regarding an index; (3) procedures that govern index determinations in periods of market stress or disruption, or other such periods where data sources may be absent; (4) procedures for dealing with error reports, including when a revision of an index would be appropriate; (5) information regarding the frequency of internal reviews and approvals (and, where appropriate, external reviews and approvals) for a methodology; (6) circumstances and procedures under which the index provider will consult with stakeholders, as appropriate; (7) the identification of potential limitations of an index, including its operation in illiquid or fragmented markets and the possible concentration of data inputs; (8) disclosure regarding any models or data extrapolation methods that are employed; and, if an index is based on data submissions, then (9) the criteria for including or excluding such data sources. *See* Principles for Financial Benchmarks Final Report, *supra* note 8, at 22-23.

[17] IOSCO Principle 12 requires that the publication: (1) clearly define what constitutes a material change, (2) explain the method and timing for consulting or notifying subscribers (and other stakeholders, where appropriate) of such change, (3) specify what the change is, (4) state when the change will apply; and (5) detail how the change will be monitored or evaluated. *See id.* at 23-24.

sufficiently detailed to allow users and potential users to assess the objectives of the index and the relevance and suitability of the index to their purposes on an ongoing basis.

Standard 6 of the Guidelines (regarding conflicts of interest) states that an index provider should adopt a conflict of interest framework that establishes clear boundaries between index calculation and maintenance and other business or commercial functional areas, as well as with the broader organizational framework.

Question 3:

How do providers analyze whether they meet the Advisers Act's definition of "investment adviser" under each element of the definition? For those providers that have determined that they meet the definition, what were the determining factors?

IIA Response to Question 3:

None of the IIA's members hold the position that they, as independent index providers, are investment advisers under the Advisers Act. We are unaware of any independent index provider that operates as a registered investment adviser.

Under Section 202(a)(11) of the Advisers Act, an "investment adviser" is: "any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities."[18] Consequently, to be an investment adviser under this provision, an entity must satisfy three factors: the person must (1) provide advice about securities (2) for compensation (3) to others.

Although the meaning of being engaged in the business of providing advisory services to others is not entirely clear on the face of the Advisers Act, the Commission has provided interpretive guidance applicable to certain service providers. For example, in determining the investment adviser status of persons who provide financial services such as financial planning or pension consulting services, the Commission has stated that such a person is engaged in the business of providing advice if it: (1) holds itself out to the public as an investment adviser or as one who provides investment advice; (2) receives any separate or additional compensation that represents a clearly definable charge for providing advice about securities; or (3) provides specific investment advice other than rarely or in isolated or non-periodic instances.[19] Commission staff has stated that a person may be viewed as holding itself out as an adviser if it: (1) advertises itself as an "investment adviser;" (2) refers to itself as an "investment adviser;" (3) maintains a listing as an investment adviser in any telephone, business, building, or other directory; (4) uses letterhead, stationery, or business cards indicating any investment advisory activity; or (5) otherwise lets it be known, through word of mouth or other means, that it is willing to provide investment advisory services.[20]

Index providers do not meet the definition of an "investment adviser" under the Advisers Act because index providers do not provide advice about securities.

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[18] 15 U.S.C. § 80b–2(a)(11).

[19] *See* Applicability of Investment Advisers Act to Financial Planners, Pension Consultants, and Other Persons Who Provide Investment Advisory Services, *supra* note 4.

[20] *See* Applicability of Advisers Act to Financial Advisors of Municipal Securities Issuers, *supra* note 5.

The term "index" is not defined in the Comment Request or in the federal securities laws generally. The IIA's official definition of an index is "a number calculated by reference to a theoretical collection of assets, market indicators, securities or derivatives whose absolute level or periodic difference relate to the performance of the theoretical collection over that period." In less technical terms, an index measures the performance, or some other characteristic, of a list of instruments (*e.g.*, bonds, stocks, commodities, derivatives) that are selected and weighted according to an employed methodology that describes a set of rules governing the construction of the index.

The purpose of an index is to represent a market segment (*e.g.*, large or small cap U.S. or global equities), asset class (*e.g.*, equity or fixed income), industry sector (*e.g.*, health care or energy), investment factor (*e.g.*, growth/value, volatility, or dividends), or other investment strategy or theme (*e.g.*, target date). Indices are designed to measure specified markets objectively, so that users of market information, particularly investors and their advisers, can make informed decisions that align with their goals. If indices were created or maintained as the index provider or another actor wished, as opposed to in accordance with specified rules and methodologies, an index may present inaccurate or inconsistent information, which would ultimately undermine investors' ability to make informed decisions, as well as the index's, and the index provider's, market credibility.

Index providers do not provide advice about securities when creating, calculating, maintaining and disseminating their indices. Specifically, the index provider does not provide any opinion or view as to whether it would be advisable for any investor to purchase or sell the securities that are components of the index during the process of creating, maintaining or licensing an index. Rather, the index provider simply administers the index as a representation of the segment of the market, a category of securities or other grouping of securities that the index was designed to represent. When constructing or rebalancing an index, the index provider does not make any judgment as to the merit of an investment in the index components. Instead, it is a mechanical procedure where all of the securities that satisfy the pre-established rules for the index are included, regardless of their investment merits.

Index providers play a key, value-creation role in the overall economy: Index providers source and process high-quality pricing and trade data to create and maintain various indices in demand by various market actors. For example, index providers license the use of their intellectual property related to the index, including the index levels and constituents, to permit asset managers to create investment vehicles and investible products that aim to mirror the performance of an index. Indices are also licensed by the active fund management industry to be used as benchmarks to compare or evaluate performance results of a particular investment strategy. These uses of indices determined by the licensee ultimately benefit investors through greater access to low-cost index-based investments, such as various index mutual funds and ETFs, and more transparent performance data in the active fund management industry.[21]

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[21] The costs associated with an index-based fund are low compared with fees associated with active management. According to a 2021 report from the Investment Company Institute, the average active equity mutual fund in the U.S. charged investors 68 basis points. By comparison, the average index equity fund charged 6 basis points. *See* James

Index providers are completely agnostic as to the approaches taken by a licensee when incorporating an index into a fund strategy or financial product design. An asset manager or fund sponsor may license an index to use as a model for an index mutual fund or ETF, or any other financial product that tracks a given market. Some licensees may choose to replicate the index in its entirety, while others may try to replicate the index through a proprietary blend of derivative instruments. Certain licensees may choose to replicate only a representative sample of the index's underlying instruments. Others may choose to impose a separate investment screen on top of a licensed index, to abide by a particular investment strategy. Still others may develop products that contain a hedge against a decline in the value of the constituents of the index or provide a measure of inverse financial exposure to them. However, in each case, the licensee, not the index provider, controls all aspects of product development and maintenance of the investment product that utilizes the index.

Additionally, index providers do not hold themselves out to the public as an investment adviser or as one who provides investment advice, do not receive any separate or additional compensation that represents a clearly definable charge for providing advice about securities, or provide investment advice. In fact, the index provider disclaims any investment advisory responsibility in connection with publishing and licensing its indices. Index providers do not manage assets or report "assets under management." Further, they do not recommend or advise on asset allocations, investment products or investment strategies.[22]

Duvall and Alex Johnson, *Trends in the Expenses and Fees of Funds, 2021*, ICI Research Perspective 28, no. 2 (Mar. 24, 2022).

[22] *See supra* note 1.

Question 6:

Which providers rely on the publisher's exclusion? On what basis? To what extent do they rely on Lowe to inform the determination? How do they determine whether their publications are "impersonal," "bona fide," or of "general and regular circulation"?

IIA Response to Question 6:

Index providers do not meet the definition of an "investment adviser" under the Advisers Act and, accordingly, are not required to register as an investment adviser with the Commission for the reasons stated in response to Question 3. Should the Commission disagree with the provided analysis and designate index providers as investment advisers, index providers are able to rely on the Publisher's Exclusion set forth in Section 202(a)(11)(D) of the Advisers Act, as interpreted by the Supreme Court in *Lowe v. SEC*.

In *Lowe*, the Supreme Court held that publishers are excluded from the definition of investment adviser under the Advisers Act as long as their publication: (1) provides only impersonal advice; (2) is "bona fide," meaning that it provides genuine and disinterested commentary; and (3) is of general regular circulation rather than issued from time to time in response to episodic market activity.[23] Thus, pursuant to *Lowe*, an index provider may rely upon the Publisher's Exclusion if the index is: (1) composed and maintained through a mechanical process that includes all qualifying securities regardless of investment merit; (2) not intended to be used for the purpose of touting particular securities; and (3) published for general use and available for licensing for any purpose.

The services that index providers provide are impersonal in nature. As discussed in the response to Question 3, indices are constructed based on a transparent, mechanical procedure where all of the securities that satisfy the pre-established rules for the index are included, regardless of their investment merits. This procedure may only be amended or altered in accordance with the index provider's documented internal procedures, pursuant to the IOSCO Principles and the Guidelines. This will be true even in instances where the index provider enters into a license agreement that grants a single sponsor of an investment product exclusive permission to operate an investment product based on an index. Moreover, IOSCO Principle 11 requires that indices are established and published in accordance with a published methodology where the index provider discloses in sufficient detail the rules governing the operation and implementation of the index.[24] Consequently, the securities included in a particular index will be selected by a pre-determined criteria and such constituent securities may only change upon a rebalance and in accordance with the methodology, rather than any individual recommendations from the index provider or a client. This is designed to ensure that personal bias has no impact in the creation and maintenance of an index.

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[23] *See Lowe v. SEC*, 472 U.S. 181, 208-210 (1985).

[24] *See* Principles for Financial Benchmarks Final Report, *supra* note 8, at 22-23.

Index providers publish each index, its methodology and related materials in a manner designed to present such information to the public as disinterested commentary. In fact, index providers will actively avoid publishing material that could be viewed as promoting or touting certain securities within an index, or as otherwise offering personalized investment advice. As discussed in the response to Question 3, indices are designed to measure specified markets objectively, so that users of an index can make informed decisions that align with their goals. If indices were created or maintained to promote certain securities, as opposed to in accordance with specified rules and methodologies, an index may present inaccurate or inconsistent information, which would not only undermine investors' ability to make informed decisions but ultimately also damage the market credibility of both the index and the index provider.

The publication of an index or other related material is of general and regular circulation. First, such information is not published time to time in response to episodic market activity. An index is constructed and rebalanced in accordance with a published methodology that is generally available to non-licensed stakeholders, including the public, as appropriate. Once an index is constructed, information about the index is published on a regular basis (*e.g.*, daily, at a set time each day). Second, access to and use of an index is generally not restricted. As explained in further detail in our response to Question 3, index providers are agnostic towards the approaches a licensee may take with respect to the design and maintenance of their funds or financial products that use an index.

Question 8:

To what extent do information providers view themselves as having fiduciary obligations to any investors that rely on the information they provide (for example, when investors receive such information through another financial professional)? How do providers view the scope of such obligations? Do they view their obligations more narrowly than those of a traditional client-facing adviser, and if so, how? How do these providers address potential conflicts of interest that may arise during their relationships with clients or users of their services?

IIA Response to Question 8:

None of the IIA's members hold the position that they, as independent index providers, have fiduciary obligations to any licensee of an index or to any customer of a licensee.

Indices are not, in and of themselves, investible products. An index simply measures the performance, or some other characteristic, of a list of instruments (*e.g.*, bonds, stocks, commodities, derivatives) that are selected and weighted according to an employed methodology that describes a set of rules governing the construction of the index. The purpose of an index is to objectively represent a market segment, asset class, industry sector, investment factor or other investment strategy or theme. At no time do index providers provide any opinion or view as to whether it would be advisable for any investor to purchase or sell the securities that are components of the index. Rather, when constructing or rebalancing an index, the index provider implements a mechanical procedure where all of the securities that satisfy the pre-established rules for the index are included, regardless of their investment merits. Consequently, there are no fiduciary obligations that arise from the creation, maintenance or licensing of indices.

The indices that are created and maintained by index providers are in demand by various market actors. For example, an asset manager or fund sponsor may license an index to use as a model for an index mutual fund or ETF, or any other financial product that tracks a given market. Indices are also frequently used by the active fund management industry as performance benchmarks. In each case, it is the licensee, not the index provider, that controls all aspects of product development and maintenance of an investment product that utilizes an index. These licensees are typically registered investment advisers or some other regulated entity that is subject to the SEC's jurisdiction, and may even owe a fiduciary duty under the Commission's regulations (*e.g.*, to the investors of a product that the licensee manages, such as a mutual fund or ETF). Consequently, adding yet another layer of regulatory oversight by designating index providers as investment advisers would not increase any protections for the end-investor while significantly increasing compliance costs.

If the Commission were to seek to redefine an index provider as an investment adviser with fiduciary duties, the duties of such an index provider with respect to a securities index that has subscribers with opposing investment goals would be confusing, contradictory and harmful to U.S. investors and the competitiveness of U.S. capital markets. In such event, there would also be significant regulatory confusion regarding the treatment of advisory clients that, in turn, owe fiduciary duties to their own advisory clients, as indicated by the Commission's questions in the

Comment Request. Further, regulatory clarity would be needed in regards to how an index provider would treat competing duties with respect to an index offered globally. For example, an index provider that licenses an index in various countries around the world would be responsible as an investment adviser with fiduciary duties to act in the best interests of each of its U.S. customers and for the same index in the U.K. and the European Union as a benchmark administrator with the duty to maintain control and independence in calculating the index according to its methodology. The result of this regulation fragmentation would be widespread confusion in:

- how the index provider should administer such a globally used index both as a fiduciary to act in the best interests of its U.S. customers and, at the same time, independently, with respect to its customers outside the U.S.;
- who the index provider's clients are from a U.S. regulatory perspective of being a fiduciary (*e.g.*, the adviser, the fund, affiliates, foreigners) and who the index provider's clients are from a non-U.S. regulatory perspective;
- the nature of the index provider's new fiduciary duties that are owed, such as a duty of care, duty of loyalty or other newly imposed obligation;
- the index provider's liability to various stakeholders both in and outside the U.S. (which would be a significant factor for index providers in determining whether they will need to price any increase in liability risk into their services to continue to offer them in the U.S. or if it makes more financial sense to discontinue such services);
- the enforceability of index provider agreements, which typically state that index providers are not investment advisers and which may cover both the U.S. and non-U.S. operations of a global asset manager under a single master agreement;
- the nature of the due diligence and ongoing monitoring that investment advisers and funds with shareholders who are U.S. persons will need to conduct on index providers, and how that will impact non-U.S. shareholders;
- whether indexed ETFs as unmanaged unit investment trusts may continue to use the services of index providers who are investment advisers;
- whether an index complies with the regulatory regime in the U.S. or that in the U.K., EU and elsewhere; and
- whether global index providers would have to separate their businesses into separate entities because the duties of an investment adviser to act in the best interests of each of its customers are incompatible with their duties of index providers under foreign regulations.

Question 9:

How do information providers exercise discretion in providing information? For example, do index providers or model portfolio providers create indexes or portfolios at the request of their licensees or users based on more customized investment objectives and goals? In these circumstances, does the provider include or exclude certain companies, funds, or countries from an index or portfolio based on the input of its licensee or user? As another example, in determining which inputs or factors to prioritize in assessing a security's price, does a pricing service prioritize certain factors over others based on the input of its licensee or user?

Question 11:

To what extent, and under what circumstances, does each type of information provider personalize the services it offers? For example, what are industry practices around direct indexing and specialized indexes, and how prevalent are they?

IIA Response to Questions 9 and 11:

Index providers may create custom indices that contain modifications that are specifically requested by a client. Like standard indices, custom indices may be broad-based (consisting of broad-based standard indices with additional requested modifications) or they may be more narrowly focused. For example, active fund managers with widely diversified portfolios found that comparisons to even an extremely broad equity index or fixed-income index may be misleading to investors because the performance characteristics of the various asset classes in their portfolio may have been purposefully selected so that they do not correlate with each other, or due to the fact that the broad index may violate one or more of their investment policy guidelines (*e.g.*, limits on individual exposures). To address this growing market need, such clients may ask index providers to produce custom indices, such as by blending together existing indices from two or more asset classes or by imposing exposure caps, that could more accurately measure the performance of their actively managed portfolios. One significant benefit of having an independent index provider create these customized performance benchmarks that include the fund manager's requested specifications, as opposed to the fund managers establishing such benchmarks themselves, is the removal of the potential conflict of interest that would occur in the latter case.

Certain index providers provide direct indexing services, which involve wealth managers and investment advisers selecting indices for their clients that they determine are suitable for their individual clients' investment needs. In providing direct indexing services, an independent index provider does not offer any investment advice, but instead it may be engaged and overseen by an investment adviser, which is solely responsible for its end-clients and for the investment services that it offers them. The investment adviser selects an index and may request additional specifications in its sole discretion and in its advisory and fiduciary capacity to its clients. The investment adviser then uses its custom index to offer its clients direct indexing services as part of the investment program managed by the investment adviser.

At no stage of the creation, maintenance or licensing of a custom index does the index provider provide any form of personalized advice or recommendation to the investment adviser or the investment company, or their clients. Further, in no event does the index provider, in connection with any custom index or direct indexing, have any assets under management or issue investable financial products. The index provider typically provides written notices to the licensees of a custom index clearly stating its limited role, including that it does not provide any investment advice. In fact, many index providers require the licensees of custom indices to provide these notices to their clients.

Question 15:

Should the Commission use its authority to exempt any of the information providers from the definition of "investment adviser"? If so, what facts and circumstances should factor into an exemption? Please explain your answer.

Question 25:

To the extent that a provider meets the Act's definition of "investment adviser," should it register with the SEC or the states in which it maintains its principal office or places of business? As a policy matter, should Commission registration be permitted or required? What economic benefits and costs would result? What would be the effect of registration on the ability of new competitors to come into the marketplace? What would be the effect of registration on providers' ability to speak or communicate? If any type of information provider were required to register, what process might we provide to ensure an orderly transition of registration status?

Question 26:

Some providers are currently SEC-registered while others are not. For each type, on what basis? For those providers that have registered with the Commission as investment advisers, what were the determining factors? How would the economic benefits and costs differ between providers that are currently SEC-registered and others that are not?

Question 30:

Should we exempt providers that meet the definition of investment adviser, and are required to register with the SEC under the Advisers Act, from any of the provisions of the Act and rules that apply to SEC-registered advisers and, if so, which provisions and why? Would any such provisions raise operational or compliance challenges such that an exemption is necessary? What would be the economic benefits and costs of exempting providers that meet the definition of investment adviser, and are required to register with the SEC under the Act? How would such an exemption affect investors? What would be the effects on competition in the market for information providers if we were to exempt providers from some or all requirements of the Act? Alternatively, should any provisions of the Act or rules apply differently to providers? Which ones, why, and how should they apply? For example, should disclosure obligations differ to the extent the providers do not have a client-facing role?

Question 31:

Would requiring providers to register with the SEC and become subject to the regulatory regime under the Act in its current form cause them to alter their business models, consolidate, or exit the market? How would this affect investors?

IIA Response to Questions 15, 25, 26, 30 and 31:

For the reasons stated in response to Question 3, none of the IIA's members hold the position that they, as independent index providers, are investment advisers under the Advisers Act. We are unaware of any independent index provider that operates as a registered investment adviser. As explained in our response to Question 6, should the Commission disagree with the provided analysis and designate index providers as investment advisers, the IIA believes that index providers are able to rely on the Publisher's Exclusion set forth in Section 202(a)(11)(D) of the Advisers Act, as interpreted by *Lowe*.

However, due to both the lack of economic benefits and the numerous, significant costs associated with designating index providers as investment advisers, as detailed in our response to Question 16, the IIA believes that the investment adviser regulatory regime under the Advisers Act is not well-suited to oversee index providers. Alternatively, the Commission could consider requiring regulated entities (*e.g.*, registered investment advisers and funds) to use index providers that adhere to the IOSCO Principles. Please see our response to Question 39 for more information on this alternative regulatory approach.

Question 16:

What are the economic benefits and costs associated with investment adviser status for each type of information provider identified above? Are there provisions of the Advisers Act that providers are unable to comply with or that would be operationally complex and burdensome?

IIA Response to Question 16:

There are no economic benefits associated with designating index providers as investment advisers. The IIA notes that the Commission's Comment Request did not raise any concerns about current index provider business practices or behaviors that are negatively impacting markets. Even Professors Mahoney and Robertson, the academics on whom the Commission relies heavily in its Comment Request, admit that "potential for index providers to exercise their discretion in self-interested ways…has not to date generated widespread abuses."[25] Instead, the Professors query: "Why shouldn't the [Commission] refrain from acting unless and until abuses occur."[26] However, the question "why not?" should not be used to justify a major rule change that would significantly, negatively impact an established, well-functioning ecosystem in the market.

In contrast, there are numerous, significant costs associated with designating index providers as investment advisers. For example, such designation would:

- Introduce friction into a well-functioning system by requiring index providers to take on fiduciary duties that they are not suited to discharge;

- Cause conflicts of interest to arise for index providers as, for any given index, they would now have to act on behalf of various advisory clients, each with differing investment goals, rather than as independent index providers;

- Bring about significant regulatory confusion, including in regards to:
    - The treatment of advisory clients that, in turn, owe fiduciary duties to their own advisory clients;
    - The enforceability of index provider agreements, which typically state that index providers are not investment advisers and are not responsible for errors;
    - whether indexed ETFs as unmanaged unit investment trusts may continue to use the services of index providers who are investment advisers; and
    - the administration of globally available indices;

- Significantly increase compliance costs for index providers, which raises the financial barrier to entry and will subsequently cause consolidation and reduce competition among index providers; and

[25] Mahoney & Robertson, *supra* note 20.

[26] *Id.* at 4.

- Most likely cause cost increases that surviving index providers and their licensees will be forced to pass onto investors[27];

Further, the resulting chill that would befall the industry would severely hamper the numerous benefits that have been brought about by indexing.

A 2021 S&P Dow Jones Indices' study estimated that indexing had generated approximately $357 billion in cumulative savings in management fees.[28] Mr. Eric Balchunas, who currently leads the ETF and passive fund research at Bloomberg Intelligence, calculated the amount U.S. investors saved due to Vanguard's introduction of the passive management strategy with the 1993 launch of the SPDR S&P 500 ETF. Mr. Balchunas found that active funds had dropped their fees from 0.99 percent in 2000 to 0.66 percent today, in large part due to competition pressures from the growing passive fund industry. Mr. Balchunas estimated that the total savings from these fee decreases to be about $200 billion. Mr. Balchunas further found that investors had less turnover expenses and other incidental savings as well, for a total estimate of $1 trillion in savings (Mr. Balchunas' findings were: $300 billion in savings related to expense ratios; $250 billion in savings related to turnover expenses; $200 billion in savings related to the decrease in fund management fees due to Vanguard's influence; and $250 billion in savings related to passive management investment strategies due to Vanguard's influence).[29]

However, should the Commission designate index providers as investment advisers and, accordingly, make it significantly more costly for index providers to operate, the resulting contraction in the industry would most likely decrease the downward market pressure on active management fees. The consequent consolidation of index providers would also likely reduce the number of available indices to investors. Additionally, the regulatory uncertainties that would arise from such designation may discourage any industry innovation in index construction, which would further reduce the number of available indices to investors.

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[27] *See supra* note 12.

[28] Ganti, *supra* note 11.

[29] Eric Balchunas, The Bogle Effect: How John Bogle and Vanguard Turned Wall Street Inside Out and Saved Investors Trillions 26 (2022).

Question 17:

To what extent are users of index providers' services registered investment companies or other pooled investment vehicles? What other types of users license indexes? Is there a difference in this respect between users of broad-based indexes and specialized indexes?

IIA Response to Question 17:

Most index licensees are financial institutions with direct fiduciary duties to their end-clients under Commission regulations or other applicable law (*e.g.*, exchanges, banks, asset managers, registered investment advisers, investment product sponsors, investment consultants, asset owners, insurance companies). Other licensees include academic institutions, research companies, corporations and media companies.

Users of broad-based indices include:

- Active funds and portfolios that are looking for general comparisons against which to measure their performance;
- Passive funds and portfolios that are looking to offer exposure to a broad representation of a given asset class or market segment; and
- Media and academics who are commenting on general market structure performance trends.

Users of custom indices include:

- Active and passive funds that are investing in a broad-based strategy or a broadly- or narrowly-defined segment of the market specifically designated by the fund sponsor or adviser to reflect the strategic focus of the fund;
- Active and passive funds with a particular investment screen; and
- Portfolio managers of separately managed accounts (SMA) who are using custom indices that are aligned with their institutional clients' unique investment guidelines (*e.g.*, rating criteria, issuer caps, sector caps) so as to have a reasonable and fair performance measurement standard.

Please see our response to Question 11 for additional information on custom indices.

Question 18:

Do index providers that develop broad-based indexes raise different investment adviser status issues as compared to those that develop customized or bespoke indexes? If so, what factors categorize or distinguish different types of indexes? Does an index that is specialized raise investment adviser status issues? Are there other parameters that we should utilize?

IIA Response to Question 18:

As explained in our response to Question 11, custom indices can be broad-based or more narrowly focused. Certain index providers offer, in addition to broad-based indices, services related to broad-based or more narrowly defined custom indices, and in each of these cases the fundamentals of the industry's indexing practices remain the same.

Operationally, once the designated market segment is conceptualized, and the index is launched, the index, regardless of whether it is standard or custom, broad-based or more narrowly focused, becomes subject to the index provider's governance framework. While custom indices reflect requested modifications specified by a client investment adviser or other institution, at no stage of the creation, maintenance or licensing of the customized index does the index provider provide any form of personalized advice or recommendation. Further, in no event does the index provider have any assets under management or issue investable financial products.

Question 19:

How, if at all, do index providers limit the dissemination of their methodologies or indexes to only those who license such information? Should the limitations placed on dissemination affect the analysis of their status as an investment adviser?

IIA Response to Question 19:

The index methodologies of the IIA members are published or accessible to all relevant stakeholders, pursuant to each member's internal policies.

IOSCO Principle 9 requires index providers to provide transparency around an index's determinations, including a published description that concisely explains the extent to which and the basis upon which discretion was used, where appropriate. Similarly, Standard 2 of the Guidelines (regarding the quality and transparency of index methodologies) requires that an index provider publish or otherwise make available the index methodologies for indices that are intended for commercial use. Standard 2 further provides that index providers should clearly document the methodology for each index intended for commercial use, to the extent practicable and allowed without violating any agreements or applicable laws restricting such publication. The published index methodology should include a description of the objective of the index and how the index is calculated and maintained. The description should be sufficiently detailed to allow users and potential users to assess the objectives of the index and the relevance and suitability of the index to their purposes on an ongoing basis.

Question 21:

What are the economic benefits and costs associated with investment adviser status for index providers that develop broad-based indexes versus specialized indexes?

IIA Response to Question 21:

Please see our detailed response to Question 11, which explains that though certain index providers offer services related to custom indices, the fundamentals of the industry's indexing practices remain the same. Like standard indices, custom indices may be broad-based (consisting of broad-based standard indices with additional requested modifications) or they may be more narrowly focused. At no stage of the creation, maintenance or licensing of a custom index does the index provider provide any form of personalized advice or recommendation to the investment adviser or the investment company, or their clients. Further, in no event does the index provider, in connection with any custom index or direct indexing, have any assets under management or issue investable financial products. As such, the economic benefits and costs associated with investment adviser status for index providers that develop custom indices would be similar to the benefits and costs for index providers that develop broad-based indices.

As discussed in our response to Question 16, there are no economic benefits associated with designating index providers as investment advisers. The IIA notes that the Commission's Comment Request did not raise any concerns about current index provider business practices or behaviors that are negatively impacting markets, including any practices or behaviors related to custom indices.

In contrast, not only are there numerous, significant costs associated with designating index providers as investment advisers but the resulting chill that would befall the index provider industry would severely hamper the numerous benefits that have been brought about by indexing.

In their law review article, which the Commission relied on heavily in the Comment Request, Professors Mahoney and Robertson acknowledge that if broad-based indices *were not to* constitute investment advice but "single purpose" indices[30] *were to* constitute investment advice, the largest global index providers would need to register as investment advisers subject to fiduciary duties, regulatory reporting, examinations and other onerous requirements, or spin off their "single purpose index businesses."[31] The IIA unequivocally disagrees with the unsupported statement by the Professors that the costs of such significant business reorganizations would be "modest." The IIA urges the Commission to consider the various substantive costs that index providers would

[30] We note that the Professors' use of the term "single purpose" index apparently refers to an index used by one client. This could be descriptive of a standard index that is developed by an index provider without input from a client which happens to be licensed by a single client, or an index with a methodology that contains a client's requested specifications that is licensed by only one client. Also under this definition, a "single purpose" index would exclude an index whose methodology contains a client's requested specifications that is licensed by more than one client (*e.g.*, custom indices that are licensed by different licensees to create the same or different types of products and to obtain constituent-level data). Thus, the term "single purpose" has limited descriptive value.

[31] Mahoney & Robertson, *supra* note 20, at 42-48.

have to face in the cost-benefit analysis for any rule proposals that may be considered and would welcome the opportunity to provide the Commission with any further information in regards to this matter.

Question 27:

Do providers have RAUM with respect to their information services? For example, do providers "provide continuous and regular supervisory or management services" to securities portfolios as required by the instructions on Form ADV for purposes of calculating RAUM? What range of RAUM is common? Should the Commission amend the Instructions to Form ADV to provide a calculation of RAUM that encompasses any or all providers? In particular, should the Commission define RAUM in a manner that explicitly applies to model portfolio providers?

IIA Response to Question 27:

Under any reasonable reading of Section 203A of the Advisers Act or the Instructions to Form ADV, index providers do not have "assets under management" or "regulatory assets under management."

Section 203A of the Advisers Act provides that, in order to register, an investment adviser must have at least a certain level of "assets under management," which is defined as "the securities portfolios with respect to which an investment adviser provides continuous and regular supervisory or management services."[32] In the Instructions for Part 1A, Item 5.F of Form ADV, the Commission clarifies that an investment adviser provides "continuous and regular supervisory or management services" if: (1) the investment adviser has discretionary authority over and provides ongoing supervisory or management services with respect to the account; or (2) the investment adviser does not have discretionary authority over the account, but has ongoing responsibility to select or make recommendations, based upon the needs of the client, as to specific securities or other investments the account may purchase or sell and, if such recommendations are accepted by the client, the adviser is responsible for arranging or effecting the purchase or sale.[33] The Instructions go on to cite the factors that should be considered in evaluating whether a person provides continuous and regular supervisory or management services to an account: (1) the terms of the advisory contract; (2) the form of compensation; and (3) management practices, or the extent to which the person actively manages assets.[34] As these factors do not apply to index providers, index providers do not have "assets under management" or "regulatory assets under management."

[32] 15 U.S.C. § 80b–3a(a)(3).

[33] *See* Form ADV Instructions at 21-24, available at https://www.sec.gov/about/forms/formadv-instructions.pdf.

[34] *Id.* at 22.

Question 28:

Should there be exemptions from the prohibition against registration for providers that have a "national presence" or can have a significant effect on the national markets regardless of RAUM? Are there factors that we should take into account in identifying those providers? For example, what characteristics would distinguish providers that have a national presence from ones that do not? Should registration be mandatory or optional? What would be the economic benefits and costs of mandatory or optional registration?

IIA Response to Question 28:

The IIA does not believe that there can be or should be exemptions from the prohibition against registration for index providers that have a "national presence" or can have a significant effect on the national markets regardless of RAUM.[35]

First, "national presence" is not an appropriate metric to use to determine registration because it is vague and subjective. Consequently, it is likely to cause confusion regarding which index providers would be required to register.

Second, requiring index providers with "national presence" or the ability to have a "significant effect on the national markets" to register as investment advisers, without any regard to the amount of RAUM the index provider may or may not have, represents a complete reversal of the Commission's (and Congress') longstanding view that entities that lack sufficient RAUM are too small to regulate as investment advisers.[36]

Due to both the lack of economic benefits and the numerous, significant costs associated with designating index providers as investment advisers, as detailed in our response to Question 16, the IIA believes that the investment adviser regulatory regime under the Advisers Act is not well-suited to oversee index providers. Alternatively, the Commission could consider requiring regulated entities (*e.g.*, registered investment advisers and funds) to use index providers that adhere to the IOSCO Principles. Please see our response to Question 39 for more information on this alternative regulatory approach.

[35] Please see our responses to Questions 25 and 27, *supra*.

[36] Section 203A of the Advisers Act generally prohibits an investment adviser from registering with the Commission unless that investment adviser has more than $100 million of assets under management. *See* 15 U.S.C. § 80b–3a(a)(2)(B)(ii)(II).

Question 29:

Under what circumstances should a provider that acts as an investment adviser be required to treat as its advisory client another investment adviser that uses its services (the "serviced adviser")? Under what circumstances, if any, should such a provider's advisory client be the client, or end-user, of the serviced adviser? If a provider's advisory client is the end-user of the serviced adviser, to what extent and under what circumstances should such end-user have the right to approve the assignment of the advisory agreement between the serviced adviser and the provider? To what extent and under what circumstances should such end-user receive the disclosure documents of the provider?

IIA Response to Question 29:

The IIA does not believe that there are any circumstances where it would be appropriate for an index provider to treat its investment adviser client as an advisory client. Imposing fiduciary duties on an index provider would cause conflicts of interests to arise as, for any given index, an index provider would have to act on behalf of various advisory clients, each with potentially differing investment goals. Such conflicts would potentially be unavoidable even if the fiduciary duties that index providers owed were limited to only investment adviser clients (which would then not be fair to the other types of clients).

Moreover, as discussed in the response to Question 3, indices are designed to measure specified markets objectively, so that users of an index can make informed decisions that align with their goals. If indices were created or maintained around certain fiduciary relationships, as opposed to in accordance with specified rules and methodologies, an index may present inaccurate or inconsistent information, which would not only undermine investors' ability to make informed decisions but ultimately also damage the market credibility of both the index and the index provider.

The IIA does not believe that there are any circumstances where it would be appropriate for an index provider to treat the index-based funds managed by investment adviser clients or the investors of an index-based financial instrument as advisory clients. As explained in our response to Question 3, it is the licensee, not the index provider, who controls all aspects of product development and the maintenance of the investment product that utilizes the index. Index providers generally do not have access to information regarding the funds that are managed by an investment adviser client or the end-investors of an index-based financial instrument, which is guarded by investment advisers as sensitive intellectual property. Consequently, in order for index providers to treat index-based funds managed by investment adviser clients or the investors of an index-based financial instrument as advisory clients, there would likely need to be a complete overhaul of well-established industry practices, which would not only increase regulatory confusion and compliance costs but also significantly hamper index innovation.

It is not clear to what extent fund boards and investors of index-based instruments would be able to evaluate and approve the assignment of an advisory agreement between an investment adviser and the index provider. Boards have experience conducting annual reviews of their funds' advisory

contracts, spending considerable amounts of time, money and effort conducting the necessary due diligence every year. Though fund boards may have a working oversight framework that could be adapted to also review and approve contracts between investment advisers and index providers, the associated costs to do so seem to significantly outweigh any benefits such additional oversight could bring, especially since investment advisers are already regulated under the same framework. Please see our response to Question 35 for more information.

Question 32:

At least one regulatory framework for index providers exists outside of the United States, under the European Securities and Market Authority ("ESMA") and its EU Benchmarks Regulation ("BMR"). Some of the BMR's key provisions include requiring EU administrators of a broad class of benchmarks to be authorized or registered by a national regulator, and for these administrators to implement various governance systems and other controls to ensure the integrity and reliability of their benchmarks. Administrators are also required to provide a code of conduct specifying requirements and responsibilities regarding input data. Although the BMR affects U.S.-based index providers that wish to have market access in the EU, it does not directly affect their business in the United States. Should any U.S. regulatory action, if adopted and implemented, be aligned with the framework placed by the BMR in the EU? Are there particular components of the BMR that should or should not be applied to index providers in the United States, and why? What has been the effect of the BMR on the provision of benchmarks and indexes in the EU? Has the BMR served as a barrier to entry for new benchmark and index providers?

IIA Response to Question 32:

The IIA believes that the EU Benchmarks Regulation (BMR), which the IIA notes is based on the IOSCO Principles, is more tailored to address the regulatory concerns applicable to index providers than the regulatory framework of the Advisers Act. Nevertheless, many index providers, including IIA members, have found implementing the BMR to be an extremely difficult challenge, in particular due to the burdensome requirements placed on non-EU index providers. In fact, the EU has twice delayed the implementation of the BMR and is currently consulting on whether a reduction in regulatory scope is necessary due to, in large part, non-EU index providers questioning the commercially viability of offering indices in the EU under the BMR. The IIA urges the Commission to consider these critical developments in the cost-benefit analysis for any rule proposals that may be considered.

The IIA represents independent index providers from around the world. Accordingly, a core tenant of the IIA's mandate is to work with regulators and other representative bodies to increase awareness of a domestic regulation's international impacts. Relatedly, the IIA notes that the Commission incorrectly states in the Comment Request that "although the BMR affects U.S.-based index providers that wish to have market access in the EU, it does not directly affect their business in the United States." It is common industry practice to not maintain separate indices for use in each jurisdiction, as that would lead to many duplicative administrative efforts and costs. As such, the BMR does, and any other similar regulations from other jurisdictions could, impact a number of U.S.-based index providers.

Another core tenant of the IIA's mandate is to work with regulators and other representative bodies to establish harmonized regulatory standards that promote business between jurisdictions. Establishing consistent international standards would provide index providers with much-needed business certainty and the ability to implement coherent international systems. More importantly, consistent international standards would increase user confidence in indices.

Due to both the lack of economic benefits and the numerous, significant costs associated with designating index providers as investment advisers, as detailed in our response to Question 16, the IIA believes that the investment adviser regulatory regime under the Advisers Act is not well-suited to oversee index providers and would be particularly disharmonious with international standards. Alternatively, the Commission could consider requiring regulated entities (*e.g.*, registered investment advisers and funds) to use index providers that adhere to the IOSCO Principles. Please see our response to Question 39 for more information on this alternative regulatory approach that is more harmonious with international standards, including the BMR.

Question 35:

How do providers analyze whether they meet the Investment Company Act's definition of "investment adviser" of a fund under each element of the definition? What are the economic benefits and costs associated with whether a provider meets the Investment Company Act's definition of "investment adviser" of a fund? Would the application of the definition to providers serve as a material barrier to entry for new entrants?

IIA Response to Question 35:

None of the IIA's members hold the position that they, as independent index providers, are investment advisers under the Investment Company Act. We are unaware of any independent index provider that operates as a registered investment adviser.

The Investment Company Act defines an "investment adviser" of an investment company registered under the Investment Company Act (a Fund) as: "(A) any person who…pursuant to contract with [a registered investment company] regularly furnishes advice to such company with respect to the desirability of investing in, purchasing or selling securities or other property, or is empowered to determine what securities or other property shall be purchased or sold by such company, and (B) any other person who pursuant to contract with a person described in clause (A) of this paragraph regularly performs substantially all of the duties undertaken by such person described in said clause (A); but does not include (i) a person whose advice is furnished solely through uniform publications distributed to subscribers thereto…."[37]

As a general rule, index providers have taken the stance that they do not meet the definition of an "investment adviser" under the Investment Company Act because index providers do not provide advice with respect to the desirability of investing in, purchasing or selling securities or other property and are not empowered to perform any of the duties undertaken by persons that provide such advice. In addition, index providers typically do not contract with an investment company directly (see responses to Questions 29 and 36), and they do not perform many of the duties undertaken by a contracted investment adviser, such as trading and portfolio management in tracking index performance; managing redemptions; serving as a fiduciary to the fund; overseeing other service providers, including broker-dealers; and, managing and implementing, in conjunction with the fund's chief compliance officer, policies and procedures designed to ensure that the fund complies with federal and state securities laws. Therefore, index providers are not required to register as an investment adviser with the Commission.

As explained in our response to Question 3, the index provider does not provide any opinion or view as to whether it would be advisable for any investor to purchase or sell the securities that are components of the index during the process of creating, maintaining or licensing an index. Rather, the index provider simply administers the index as a representation of the segment of the market, a category of securities or other grouping of securities that the index was designed to represent. When constructing or rebalancing an index, the index provider does not make any judgment as to

[37] 15 U.S.C. § 80a–2(a)(20).

the merit of an investment in the index components. Instead, it is a mechanical procedure where all of the securities that satisfy the pre-established rules for the index are included, regardless of their investment merits.

Since an index provider that is considered to be an investment adviser to a registered investment company under the Investment Company Act would be subject to the regulatory requirements under Advisers Act, please see our response to Question 16, which details the lack of economic benefits and the numerous, significant costs associated with designating index providers as investment advisers.

To the extent an index provider is an investment adviser to a registered investment company, its contracts with investment advisers may be subject to board approval under Section 15(c) of the Investment Company Act.

Section 15(a) of the Investment Company Act provides that it is unlawful for any person to serve or act as investment adviser of a registered investment company, except pursuant to a written contract, which has been approved by a vote of a majority of the outstanding voting securities of the registered investment company and may continue in effect for a period of more than two years from the date of its execution only so long as such continuance is specifically approved at least annually by the board of trustees or by a vote of a majority of the outstanding voting securities of such company. Section 15(c) of the Investment Company Act requires that every investment advisory contract for a registered investment company, initially and upon each renewal, be approved by a vote of a majority of the independent trustees.[38] In connection with these approvals, trustees must request and evaluate "such information as may reasonably be necessary to evaluate the terms of any [such] contract."[39]
The obligations of independent trustees in evaluating advisory contracts under Section 15(c) of the Investment Company Act are primarily derived from court opinions in cases brought under Section 36(b) of the 1940 Act, which imposes on the investment adviser a fiduciary duty "with respect to the receipt of compensation for services, or of payments of a material nature," paid by the investment company or its shareholders to the adviser or any affiliated person of the adviser.[40] The *Gartenberg* standard, first articulated by the U.S. Court of Appeals for the Second Circuit, mandates an assessment as to whether the compensation paid to an adviser is "so disproportionately large that it bears no reasonable relationship to the services rendered and could not have been the product of arm's-length bargaining."[41] In judging whether this standard has been met, the courts have stated that "all pertinent factors must be weighed."[42] The *Gartenberg* Court stated that a board should consider, at a minimum, the following factors (often referred to as the *Gartenberg* factors): (1) the nature and quality of the services to be provided; (2) the extent to which economies of scale have been taken into account in setting the fee schedule; (3) the existence of "fall-out" benefits to the adviser; (4) the

[38] An "independent trustee" is a trustee who is not an "interested person" of an investment company, as that term is defined in Section 2(a)(19) of the Investment Company Act.

[39] 15 U.S.C. § 80a–15(c).

[40] 15 U.S.C. § 80a–35(b).

[41] *Jones v. Harris Associates, L.P.*, 559 U.S. 335 (2010).

[42] *Gartenberg v. Merrill Lynch Asset Management, Inc.*, 694 F.2d 923, 929 (2d Cir. 1982).

comparison of advisory fees to those of similar funds; and (5) the profitability of the advisory business to the fund adviser.[43] Consequently, such an analysis would cause fund boards and index providers to incur substantial compliance costs.

Meanwhile, the resulting benefit would be minimal since investment advisers (who, as explained in our response to Question 3, control all aspects of product development and maintenance of the investment product that utilizes the index) are already regulated under the same framework. Moreover, increased compliance costs would introduce significant barriers that will lead to higher consolidation and less competition in both the index and fund industries and, ultimately, a reduction in the number of available investment products to investors.

The Commission's suggestion in the Comment Request that an index provider could implicate the Investment Company Act's definition of investment adviser of an investment company, including when the index provider does not contract directly with the fund but, instead, indirectly with the fund's investment adviser, may be a reference to, or borrows from, the argument put forth by Professors Mahoney and Robertson in their article, *Advisers by Another Name*, which is cited in footnote 4 of the Comment Request. Specifically, the Professors state:

> While this would seem to take the index provider out of the scope of clause (A) of the definition, the inquiry does not end there. The [Commission] and the federal courts, in other contexts, have refused to give a strict meaning to analogous terms suggesting contractual privity. For example, Section 12(a)(1) of the Securities Act of 1933 confers a private right of action for violations of the statute's registration and prospectus delivery requirements on 'any person purchasing such security from' the violator. The Supreme Court, however, concluded that this language does not require that the defendant transfer title directly to the plaintiff.[44]

However, the Professors' argument is inapposite and specious. In the case cited, *Pinter v. Dahl*, the court was merely stating that a vaguely and broadly written phrase could contemplate many actors.[45] So, in that case, the definitions under Section 2(3) of the Securities Act of 1933 of "sale" or "sell" to include "every contract of sale or disposition of a security or interest in a security, for value," and the terms "offer to sell," "offer for sale," or "offer" to include "every attempt or offer to dispose of, or solicitation of an offer to buy, a security or interest in a security, for value" contemplate that the range of persons potentially liable under §12(1) under the Securities Act of 1933 is not limited to persons who pass title. The important difference here is that the Investment Company Act provides that a specifically designated contractual party must be a fund. The words of the Investment

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[43] A sixth factor identified in *Gartenberg* suggests that a board should consider the volume of transactions that must be processed. This factor was relevant in *Gartenberg* because that case involved a money market fund and the Court considered that the adviser's brokerage affiliate had to process a "huge number of daily orders" inherent to a retail money market fund. Thus, this factor may only be relevant in limited circumstances.

[44] Mahoney & Robertson, *supra* note 20, at 36-37.

[45] *See Pinter v. Dahl*, 486 U.S. 622 (1988).

Company Act in this regard are not nebulous, vague or subject to broad interpretation of who must be a party to an advisory contract.

Question 36:

To what extent do providers contract directly with funds? For example, do providers typically enter into contracts with the fund's adviser, or an affiliate of the adviser? If a fund's adviser delegates services to a provider, what duties does the adviser retain and what duties does the adviser delegate? Does the fund or its adviser make an affirmative determination made whether the provider is acting as an investment adviser under the Investment Company Act?

IIA Response to Question 36:

Index providers generally do not directly contract with funds. As explained in our response to Question 29, the accepted industry practice is for index providers to enter into contracts with a fund's investment adviser.

Investment advisers do not delegate any duties to index providers. Instead, investment advisers pay index providers to obtain an intellectual property license that allows the investment adviser to use the index and any related data for commercial use. As described in our response to Question 3, the investment adviser, as the licensee, controls all aspects of product development and maintenance of the investment product that utilizes the index. Notably, active fund managers do not typically hold all the securities included in their benchmark index and will often hold securities that are not part of the index. Furthermore, two passive index funds tracking the same index may not hold the same securities, highlighting the fact that each fund manager is individually in control of the ultimate investment decisions made on behalf of the fund.

Accepted industry norms assume that the index provider is not an investment adviser under the Investment Company Act. In fact, index provider agreements typically state that index providers are not investment advisers and are not responsible for errors. Accordingly, the IIA is unaware of any fund or investment adviser that has determined that an index provider is acting as an investment adviser under the Investment Company Act.

Question 37:

The Investment Company Act excludes from the definition of investment adviser of a fund "a person whose advice is furnished solely through uniform publications distributed to subscribers thereto." To what extent do providers distribute uniform publications? If so, how do these providers interpret "uniform"? Do providers that rely on the Advisers Act publisher's exclusion also rely on this exception and, if so, on what basis?

IIA Response to Question 37:

As discussed in more detail in our response to Question 35, IIA believes that index providers do not meet the definition of an "investment adviser" under the Investment Company Act because index providers do not provide advice with respect to the desirability of investing in, purchasing or selling securities or other property and are not empowered to perform any of the duties undertaken by persons that provide such advice. To the extent index providers are considered investment advisers under the Investment Company Act, qualifying index providers would rely on the "uniform publication" exclusion that is available under the Investment Company Act.

Question 38:

To the extent a provider to a fund is an investment adviser of the fund, the fund and its provider would need to comply with various provisions of the Investment Company Act. What would be a reasonable amount of time for a registered investment company to come into compliance with these provisions? Are there measures we can take to assist with the transition? Are there provisions of the Investment Company Act that present unique challenges for providers?

IIA Response to Question 38:

As explained in our response to Question 35, IIA believes that index providers do not meet the definition of an "investment adviser" under the Investment Company Act. To the extent an index provider is an investment adviser to a registered investment company, regulating index providers as investment advisers under the Investment Company Act would create significant compliance challenges and would fundamentally disrupt the index industry.

For example, conflicts of interest would necessarily arise for index providers with indices that are used by multiple funds, especially if those funds have differing investment goals. There would also be logistical challenges in terms of identifying all of the funds that the index provider would now have to treat as advisory clients. This is because index providers generally do not have access to information regarding the funds that are managed by an investment adviser client. Consequently, in order for index providers to treat index-based funds managed by investment adviser clients as advisory clients, there would likely need to be a complete overhaul of well-established industry practices, which would not only increase regulatory confusion and compliance costs but also significantly hamper index innovation.

Additionally, to the extent an index provider is an investment adviser to a registered investment company, its contracts with investment advisers may be subject to board approval under Section 15(c) of the Investment Company Act. This would cause fund boards and index providers to incur substantial compliance costs related to (1) obtaining board approval of index license agreements, including by submitting or presenting sufficient materials to satisfy a *Gartenberg* analysis; (2) obtaining board approval of the index provider's compliance framework; and (3) regularly attending fund board meetings and submitting reports to the fund board.

Designating index providers as investment advisers to registered investment companies would also cause the index providers to become affiliated persons to those registered investment companies, pursuant to Section 17 of the Investment Company Act, which would cause even more regulatory confusion for index providers.

Question 39:

Rule 38a-1 under the Investment Company Act requires a fund's board, including a majority of its independent directors, to approve policies and procedures reasonably designed to prevent violation of the Federal securities laws by the fund and certain service providers. To what extent do funds currently extend their compliance program to information providers, where such entity is not considered an investment adviser or one of the rule's other named service providers (principal underwriters, administrators and transfer agents)? Does this analysis differ depending on the provider? Should we amend Rule 38a-1 to incorporate information providers within a fund's compliance program, rather than requiring registration of information providers as investment advisers? What would be the costs and benefits of such an approach?

IIA Response to Question 39:

Many IIA members are routinely reviewed by investment advisers in regards to their internal controls as part of those investment advisers' due diligence on service providers. Some IIA members even provide public statements of adherence with detailed descriptions of their control frameworks to funds, asset managers and other users of their indices, with internal or external auditors often conducting assessments of the controls described in these statements.

The many index providers who adhere to the IOSCO Principles commit to appointing an internal or external auditor with appropriate experience and capability to periodically review and report on the index provider's adherence to the IOSCO Principles and internal policies, pursuant to IOSCO Principle 17. Further, every IIA member commits to complying with the IIA Guidelines, which similarly provide, under Standard 10, that an index provider's compliance be subjected to appropriate review on a periodic basis.[46]

IIA is generally supportive of initiatives that seek to incorporate review of index providers and their control frameworks into a fund's or investment adviser's compliance program. Having funds and investment advisers review an index provider's index governance, operations, business continuity plans, cyber security, business code of ethics and compliance framework is a sound potential alternative to address the Commission's concern of protecting fund shareholders without imposing undue regulatory burdens and increased compliance costs on index providers. Investment advisers, in particular, are well-suited for this role, as they already play a key role in index provider selection and are familiar with index provider contract terms, associated fees and the process of monitoring index performance. As such, it should not be necessary to have a fund oversee an index provider where its investment adviser does so.

To ensure that such reviews do not become too burdensome for funds and investment advisers, any rule adopting this approach should clarify that an internal or external audit report in adherence to IOSCO Principle 17 would satisfy the review requirement except in certain extenuating circumstances (*e.g.*, the fund or investment adviser becomes aware of a significant control failure that the fund or investment adviser believes warrants further investigation).

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[46] *See supra* note 13.