

# The Role of Alternative Investments in Today's Capital Markets

A White Paper by Managed Funds Association



# MANAGED FUNDS ASSOCIATION

## THE VOICE OF THE GLOBAL ALTERNATIVE INVESTMENT INDUSTRY

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MFA is the leading voice of the global alternative investment industry and its investors – the public and private pension funds, charitable foundations, university endowments and other institutional investors that comprise more than 65 percent of our industry’s assets. Collectively, MFA Members manage more assets than any other hedge fund trade association. Our global network spans six continents and includes more than 13,000 individuals.

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**ADVOCATE** - We promote public policies that foster efficient, transparent and fair capital markets. With the strategic input of our Members, we work directly with legislators, regulators and key stakeholders in the U.S., EU and around the world.

**EDUCATE** - Each year we hold more than 100 conferences, forums and other events that give our Members the tools and information they need to thrive in an evolving global regulatory landscape. Our expertise has additionally been recognized by policymakers, who consistently reach out to our team for insight and guidance.

**COMMUNICATE** - We tell the story of an industry that creates opportunities and economic growth. Through outreach to journalists and thought leaders, we inform coverage of our industry and highlight the work our Members do to provide retirement security for workers, capital for businesses, and increased resources for endowments and foundations.

To learn more about us, visit [www.managedfunds.org](http://www.managedfunds.org).



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# THE ROLE OF ALTERNATIVE INVESTMENTS IN TODAY'S CAPITAL MARKETS

## I. FOREWORD

by Richard H. Baker



It has been more than five years since Congress passed the Dodd-Frank Act, a sweeping set of reforms intended to modernize the regulatory framework of the U.S. financial system and give regulators new tools to help make future crises less likely and less damaging. While not every aspect of the landmark law has been fully implemented, it has had a profound effect on capital markets and market participants.

As the leading voice for the alternative investment industry, Managed Funds Association played a meaningful role throughout the legislative process by providing constructive feedback to policymakers on ways to ensure a safer, more stable and more transparent post-crisis financial system. MFA has continued to engage policymakers since the passage of the Dodd-Frank Act to accomplish those shared goals while also advocating for the alternative investment and broader asset management communities.

MFA's leadership – our Board of Directors, the members of MFA's Founders Council and the leaders of our various substantive policy committees – has always been clear: Our role is to be a constructive advocate for fair, efficient and liquid capital markets, and serve as a policy steward for our industry, its professionals and the investors they serve. This is why MFA has embraced many financial market reforms contained in the Dodd-Frank Act.

Although no hedge fund required a government bailout during the recent – or any past – financial crisis, the industry has evolved its business practices to adapt to recent reforms, often going beyond what is mandated by law. Today, the industry is part of the globally regulated financial mainstream and is more transparent than it has ever been. Furthermore, firms across the industry have vastly improved their ability to manage risks for their firms and on behalf of their investors.

Despite changes to the industry and financial regulation, many people still hold antiquated and inaccurate views of what the alternative investment community does and the role the industry and its professionals play in the financial ecosystem. It is for that reason that I am pleased to present *The Role of Alternative Investments in Today's Capital Markets*. As the paper details, today's well-regulated hedge fund industry plays an active and dynamic part in capital markets as well as a critical role in the global economy.

## II. EXECUTIVE SUMMARY

This report provides an examination of the regulatory framework that has been implemented in the U.S. since the global financial crisis. It also discusses the important role alternative investments like hedge funds play in this new, tightly-regulated, post-crisis economy.

While special attention will be given to the changes brought about by the Dodd-Frank Act, it is important to note that other jurisdictions have similarly adopted robust regulatory regimes for alternative investment and private fund managers, including the European Union's (EU) adoption of revisions to the Markets in Financial Instruments Directive (MiFID), the Alternative Investment Fund Managers Directive (AIFMD) and the European Market Infrastructure Regulation (EMIR).

Combined, these new laws and regulations reach every corner of our global economy. Large banks now face new risk retention rules for securitization, capital rules and new mortgage requirements. This has, in many cases, contracted bank lending. Alternative investments have started to fill that vacuum in the U.S., EU, and most recently, in Asia.

The emergence of alternatives in capital markets highlights the important and expanding role private funds play in the global economy. This paper explores how funds operate in this new role, focusing on the tools used by fund managers to manage risk, provide reliable returns over time and offer portfolio diversification. Importantly, the paper also explains how funds do this without posing systemic risk to the broader financial system or investors.

With approximately \$3 trillion dollars in global assets under management, the hedge fund industry is relatively small in size when compared to the size and scale of the overall financial system. The industry is also significantly less concentrated than other parts of the financial services industry and its transparency is at an all-time high.

Hedge funds have become part of the financially regulated mainstream. In the U.S., Europe and beyond, regulators now have extensive oversight of hedge fund managers and an array of information about their activities. In the U.S., large managers must register with the Securities and Exchange Commission and the Commodity Futures Trading Commission. They also file extensive reports about their portfolios and counterparty exposures with those agencies. Small fund managers are subject to state registration, examination and reporting requirements.



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*“The Dodd-Frank Act, combined with financial regulations in the EU, has changed the way our financial and capital markets function and brought forth a new economy that is more regulated, more transparent, and more reliant on alternative investment vehicles like hedge funds to provide capital.”*

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The market activities of every U.S.-based hedge fund are subject to U.S. securities and commodities laws. In addition, hedge funds execute trades and obtain other services from prime brokers (banks), which are also subject to extensive regulation that indirectly affects hedge fund activities.

The Dodd-Frank Act, combined with financial regulations in the EU, has changed the way our financial and capital markets function. These reforms have brought forth a new economy that is more regulated, more transparent and increasingly reliant on alternative investment vehicles like hedge funds to provide capital to businesses and liquidity to markets.

## Key Takeaways

This report examines the role hedge funds play in a post-crisis global economy. The following key takeaways provide a more detailed understanding of the hedge fund industry and its investors, as well as clarify several common misunderstandings.

- Hedge funds are no longer just tools for high-net worth individuals. Today, institutional investors now represent nearly two-thirds of the industry's assets under management. Fund managers are trusted partners of pension funds, charitable foundations and university endowments that help these organizations fulfill their fiduciary obligations and meet financial goals.
- Hedge funds are part of the financially regulated mainstream. Fund managers and their activities are monitored by the SEC and CFTC in the U.S. and well-regulated by several EU regulatory laws and individual Member State authorities.
- The hedge fund industry is more transparent than ever before. Fund managers report detailed information about their funds to regulators and investors.
- As new regulations have constrained the lending capabilities of banks, hedge funds have stepped in to provide capital for local communities and businesses working to expand and create jobs.
- The U.S. systemic risk regulator, FSOC, has acknowledged that “asset management firms and investment vehicles have closed without presenting a threat to financial stability.” In fact, the very nature of the industry prevents it from posing a systemic risk for the following reasons:
  - **Relative Size:** Hedge funds' approximately \$3 trillion in AUM represents a fraction of broader markets.
  - **Less Concentration:** The hedge fund industry is far less concentrated than other parts of the financial services industry, making it unlikely that the closing of any one fund would cause a systemic risk. Only a few hedge fund firms have more than a one percent market share of the industry's total AUM, and no hedge fund has more than 10 percent – small percentages when compared to other members of the financial system.
  - **Diverse Investment Strategies:** Hedge funds pursue a tremendous diversity of investment strategies and invest in a wide range of asset classes that are often not correlated to the broader markets or each other.
  - **Less Leverage:** Data shows that hedge funds are less leveraged than many other types of financial institutions.

### III. INDUSTRY OVERVIEW

The investor makeup of the hedge fund industry has evolved in recent years. In the 1980s, institutions of higher learning began partnering with funds as a way to help fund scholarships, cutting-edge research and infrastructure upgrades. This institutional partnership expanded in the 1990s and early-2000s to include public and private pension funds. Now, philanthropic foundations also partner with hedge funds to help achieve their missions.

Today approximately 65 percent of all hedge fund assets under management come from these institutional investors.

Globally, the hedge fund industry has approximately \$3 trillion in assets under management.<sup>1</sup> Nearly two-thirds of this capital belongs to the more than 4,800 institutional investors who depend on hedge funds as a tool to diversify their portfolio, protect against market fluctuations, and provide risk-adjusted returns over time.<sup>2</sup> In fact, 80 percent of investors believe their portfolio risk would increase if hedge funds were removed from their portfolios, according to one independent survey.<sup>3</sup> Preqin, a leading research firm, found that institutional investor satisfaction with hedge funds is high. Those surveyed even indicated that they plan to maintain or increase existing allocations.

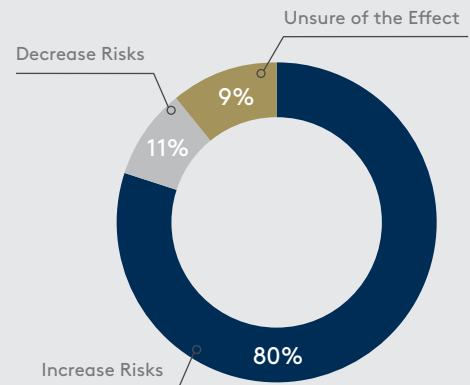
While hedge funds have grown in popularity, they represent a relatively small part of the asset management industry. For example, the hedge fund industry is less than a tenth of the size of the global mutual fund industry, which managed more than \$31 trillion at the end of the 2014 fiscal year.<sup>4</sup> In addition, there are five U.S. bank holding companies that each individually have assets equal to 50 percent or more of the entire U.S. hedge fund industry's AUM.<sup>5</sup>

The hedge fund industry is also not concentrated by any measure. Only a few firms have more than a one percent market share of the industry's total AUM, and every firm is well below 10 percent. In fact, it takes 100 firms together to reach approximately 50 percent of the total AUM managed by the industry.

Amidst changes in size and industry makeup, several facets about hedge funds remain the same – including limits on who can invest in them and how they are structured.

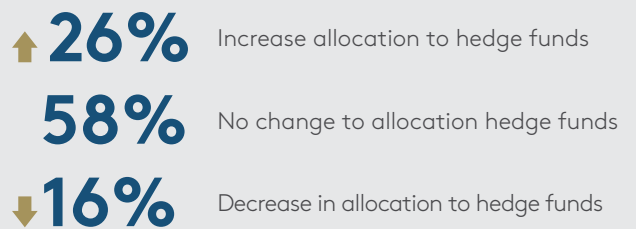
1 HFR, "Global Hedge Fund Industry Report, First Quarter 2015," Estimated Annual Growth of Assets/Net Asset Flow, April 2015  
 2 Preqin, "2015 Preqin Global Hedge Fund Report," Investors & Gatekeepers, February 2015  
 3 Preqin, "Special Report: The Real Value of Hedge Fund Investments," June 2014  
 4 Investment Company Institute, worldwide Mutual Fund Assets and Flows Third Quarter 2014, December 2014  
 5 National Information Center, Holding Companies with Assets Greater than \$10 Billion, Federal Financial Institutions Examination Council, March 2015

**80%** of investors believe their portfolio risk would increase if hedge funds were removed from their portfolios, according to a recent survey.



**65%** of hedge fund industry capital comes from institutional investors

#### Among Recently Surveyed Investors



It takes **100** firms together to reach approximately **50%** of the total AUM managed by the industry

U.S. regulations generally limit investment in hedge funds to “accredited investors” or “qualified purchasers.” The former is defined as individuals with a net worth of at least \$1 million, not including the individual’s primary residence, or income of at least \$200,000 in the last two years and institutions with more than \$5 million in assets. The latter refers to individuals with at least \$5 million in investments or institutions with at least \$25 million in investments.

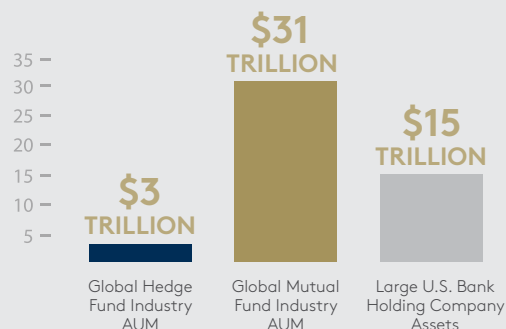
Hedge funds are generally structured as partnerships, limited liability companies, or similar entities where investors hold a percentage of shares in the fund along with the manager who also invests in the fund. Since managers are invested in their fund, he or she has a significant amount of money at stake with every investment decision. This is often referred to as “skin-in-the game.”

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S&P 500 and other public indices are commonly seen as irrelevant - just a fifth compare hedge funds to these benchmarks



Investors commonly use strategy-specific hedge fund indices to measure portfolio performance.



#### IV. THE ROLE OF ALTERNATIVES IN CAPITAL MARKETS

Since the financial crisis, government regulations have brought hedge funds into the financial mainstream. Increasingly, pension funds, college endowments, and non-profit foundations use hedge funds as tools to fulfill their fiduciary obligations or help meet their financial goals.

Endowments, to a large degree, led the way for institutional investors to begin making hedge fund allocations. Public pension funds, on the other hand, are relatively new investors in the hedge fund asset class, but now account for four of the top five hedge fund investors in North America. A state-run university endowment plan completes that list.<sup>6</sup>

U.S. based endowments, foundations and private sector pension plans also account for the majority of the global top five list of hedge fund investors in their respective categories.

A plurality of investment officers at these institutions look to hedge funds to provide risk-adjusted returns over time. Nearly 40 percent report depending on their hedge fund allocations to dampen market volatility and provide returns uncorrelated to equity markets.<sup>7</sup>

Institutional investors, however, are not the only entities that use hedge funds as a tool to meet their financial objectives. Since banks have seen their lending limits constrained through new capital and liquidity requirements under the Dodd-Frank Act<sup>8</sup> and Basel III requirements, many small and medium-size businesses are turning to hedge funds to provide alternative lending options. This type of financing specifically helps small and medium-sized enterprises get off the ground by efficiently and effectively allocating capital, providing businesses access to financing, creating jobs and broadening the tax base.

The private debt industry globally has an estimated \$154 billion in committed capital ready to be invested, according to one research group, and has a total AUM of \$500 billion. This type of investing increased 23 percent from 2013 to 2014 in Europe alone.<sup>9</sup>

<sup>6</sup> Prejin, “2015 Global Hedge Fund Report,” Investors & Gatekeepers, February 2015

<sup>7</sup> Prejin, “2015 Global Hedge Fund Report,” Investors & Gatekeepers, February 2015

<sup>8</sup> Department of the Treasury Office of the Comptroller of the Currency, 12 CFT Parts 32, 159 and 160, Docket ID OCC-2012-0007, RIN 1557-AD59, Lending Limits, June 2013

<sup>9</sup> Prejin, “2015 Global Private Debt Report,” March 2015



## V. INCREASED TRANSPARENCY

The alternative investments industry has become considerably more transparent to regulators since the financial crisis. Title IV of the Dodd-Frank Act specifically addresses the regulation of hedge fund advisers and other private fund managers. As a result, hedge funds provide detailed information directly to the SEC and CFTC. That information is also available to FSOC and the Office of Financial Research (OFR), both created by the Dodd-Frank Act.

The Dodd-Frank Act created multiple thresholds for adviser registration and regulatory examinations at the national and state levels. The most significant threshold for private fund advisers is \$150 million in AUM, which requires the adviser to register with the SEC. Advisers with less than \$100 million in AUM generally are required to register with state regulatory agencies. Many advisers to private funds also must register with the CFTC as commodity trading advisers (CTAs) or commodity pool operators (CPOs).

All SEC-registered advisers report firm-specific information to the SEC with annual Form ADV filings. The first part of the ADV form collects information on ownership, clients, employees, business practices, and affiliations. Managers report information like fee structures, types of services offered, and potential conflicts of interest on the second part of the form. The completed forms, which 95 percent of investors report they plan to review,<sup>10</sup> are available on the Investment Adviser Public Disclosure website.

The SEC also requires the filing of Form PF, which requires advisers with at least \$1.5 billion in hedge fund AUM to comply with substantial SEC regulatory reporting requirements. The CFTC requires CPOs and CTAs to submit Form CPO-PQR and Form CTA-PR to the National Futures Association (NFA).<sup>11</sup>

For large firms, these forms are required on a quarterly basis. Taken together, the forms help regulators monitor fund holdings and strategies in order to evaluate the use of leverage and review asset/liability and liquidity matching.

The Dodd-Frank Act gives FSOC and OFR access to all reports and information filed with or provided to the SEC in order to assess systemic risk. Moreover, the Dodd-Frank Act gives the Director of the OFR subpoena power<sup>12</sup> to obtain from any bank or non-bank institution, including hedge funds, any data needed to carry out the functions of the office. With access to

unlimited information and data, regulators have the authority to analyze the entire hedge fund industry and all aspects of a particular hedge fund's investment activities, including market and counterparty exposure.

Lastly, small fund managers are subject to state registration, examination, and reporting requirements.

The market activities of every U.S.-based hedge fund are subject to U.S. securities and commodities laws.



*“The market activities of every U.S.-based hedge fund are subject to U.S. securities and commodities laws.”*

10 Deutsche Bank Global Prime Finance, Third Annual Operational Due Diligence Survey, Summer 2014

11 NFA was founded in 1982 as a self-regulatory organization for the U.S. derivatives industry with mandatory membership.

12 H.R. 4173, Sec. 153 (f)

## VI. IMPROVED RISK MANAGEMENT

Hedge funds rely on investor contributions and borrowed funds to create their overall portfolio. Managers work to match investor contributions and borrowed funds to the liquidity of the assets and overall investment portfolio. This is intended to ensure that market volatility does not put the fund or its investors at risk.

The industry has developed practices to manage liquidity risks.<sup>13</sup> One of those practices is generally using secured borrowings instead of relying on unsecured, short-term financing. With secured borrowing, funds pledge collateral of cash or securities that are marked-to-market on a daily basis. The U.K. Financial Conduct Authority's Hedge Fund Survey released in 2014 and the SEC staff's 2013 Form PF report confirmed these practices.

Many of the largest hedge funds invest primarily in highly liquid, exchange-traded equities, debt, futures, and other instruments. For these funds, monthly or quarterly redemption does not pose significant liquidity risk. Private funds that invest primarily in fairly illiquid assets (for example, high yield bonds and senior debt securities) manage their liquidity risk by, among other things, utilizing contractual redemption restrictions and other management tools available to them.

Funds conduct regular liquidity stress tests to verify their portfolios can meet investor obligations as well as to respond to financing obligations and market conditions.

Another unique aspect of hedge funds is that they are not subject to mandatory redemption requirements under any statute or regulation. Their organizational documents generally impose certain limits on investors' ability to redeem their interests. This gives managers the ability to ensure that liquidity of the fund's portfolio is consistent with their funds' redemption obligations.<sup>14</sup>

As noted earlier, hedge funds utilize borrowed funds to complement investor assets. This practice has led some to reach the false assumption that hedge funds are highly leveraged. Funds are, in fact, often much less leveraged than other financial institutions. One study examining leverage ratios between December 2004 and October 2009, a period encompassing the height of the economic crisis, found the average leverage ratio was 2.1x.<sup>15</sup> This compares to average ratios of approximately 13x for the U.S. banking industry<sup>16</sup> and 11.8x for the insurance industry<sup>17</sup> over the same timeframe.

All funds have unique leverage ratios to achieve their investment strategies and some use greater leverage than others, but funds typically engage in collateralized financing that requires daily margining. This means that if a fund closes or experiences significant losses, its creditors are protected because they have legal rights to seize fund assets. It also is

<sup>13</sup> MFA, Sound Practices for Hedge Fund Managers, 2009

<sup>14</sup> Office of Financial Research, Annual Report, 2013

<sup>15</sup> Andrew And, et al., Hedge Fund Leverage, National Bureau of Economic Research, Working Paper No. 16801, 2011

<sup>16</sup> Sebnem Kalemli-Ozcan et al., Leverage Across Firms, Banks and Countries, National Bureau of Economic Research, Working Paper 17354, 2011

<sup>17</sup> Federal Insurance Office, Annual Report on the Insurance Industry, June 2013

### Average Leverage Ratios between December 2004–October 2009



important to realize that funds can use leverage as a tool to mitigate risks to the overall portfolio.

These safeguards are ultimately tested multiple times each year when funds close for reasons ranging from extended poor performance, the retirement or departure of senior personnel, or a changed market environment. In each case, the fund's portfolio is wound down by the manager, sometimes gradually over many months and less frequently in a "liquidation" by the prime brokers or other market participants that hold the fund's collateral. But, compared to other types of financial institutions, hedge fund managers generally operate straightforward businesses with limited exposure to other financial institutions. Because of their simple legal structure, hedge funds are easily wound down and liquidated under existing bankruptcy laws, limiting losses to the fund's investors and generally not creditors or counterparties.

This happened during the financial crisis without any government intervention. FSOC has even recognized that "asset management firms and investment vehicles have closed without presenting a threat to financial stability."<sup>18</sup>

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*FSOC: "Asset Management Firms and Investment Vehicles Have Closed Without Presenting a Threat to Financial Stability."*

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Threats to fund sustainability are not limited to market factors. Managers must also deal with operational risks the same as other businesses. These risks include human error, natural disasters, counterparty failure and the increasing threat of cyberattack. SEC rules require each manager to adopt business continuity plans to address risks that could impact the manager's ability to manage clients' money. Successful fund managers are constantly evaluating and adopting procedures to address vulnerabilities.

Investors themselves, however, are perhaps the most important risk management factor for hedge fund managers. Pursuant to federal securities laws, hedge fund allocations are available only to large institutions and high-net worth investors. These professionals have long-term investment horizons and do not view their hedge fund investments as temporary placements requiring immediate access. These investors typically invest in hedge funds to diversify portfolio risk and to minimize exposure to market fluctuations – and they pay close attention to fund managers' risk management and operational practices.

Investors and third-party consultants spend considerable time before investing. This due diligence process typically takes months to complete.<sup>19</sup> Detailed diligence questionnaires, in-person interviews, and third-party background and reference checks are all used to examine business operations and risk practices often before any decision to invest in a hedge fund is made.

Investors and consultants continue to focus on these issues as part of ongoing due diligence, even after an initial investment is completed.

### ***Is the Near-Failure of Long-Term Capital Management (LTCM) in 1998 a Useful Case Study for Financial Regulators Exploring Systemic Risk?***

In light of the many regulatory and market changes over the last 15 years, the LTCM event is an outdated example of hedge fund risk.

As has been extensively documented, LTCM's excessive position size and leverage, along with its counterparties' inadequate risk management, were the primary underlying causes of LTCM's closing. The seminal analysis of the matter, conducted by the President's Working Group on Financial Markets, found that LTCM, as of January 1, 1998, was leveraged more than 25-to-1 and that LTCM was able to get such leverage because its counterparties did not require LTCM to post initial margin on its over-the-counter derivatives or "OTC" trades.

Prior to the 2008 financial crisis, counterparties generally revised their policies to require posting of initial margin on OTC trades, a practice the Dodd-Frank Act codifies.

Finally, despite initial concern from regulators, there was no actual impact on taxpayers or retail investors from the LTCM closure. While Federal regulators coordinated a private sector solution, importantly, there was no taxpayer bailout of LTCM.

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<sup>18</sup> FSOC Notice Seeking Comment on Asset Management Products and Activities, Docket No. FSOC-2014-0001

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<sup>19</sup> Deutsche Bank Global Prime Finance, Third Annual Operational Due Diligence Survey, Summer 2014

## VII. CONCLUSION

This paper has examined the role alternative investments play broadly in our new economy and has specifically focused on the regulatory changes brought about in response to the financial crisis. Now, several years removed from the crisis and more than five years into the Dodd-Frank Act, economic recovery is beginning to take hold in the U.S.

Looking back, it is important to note that while funds have, at times, liquidated their assets and wound down for various reasons, no hedge fund has required a taxpayer bailout and the industry has never required a government program such as the Troubled Asset Relief Program or similar government backstop.

The hedge fund industry instead advocated for and embraced broad market reforms and is vastly different than it was in 2007 when the financial crisis began.

Significant regulatory changes have been implemented and market practices have fundamentally changed the way funds invest and manage risk. Hedge funds are more transparent than ever before. Managers have accepted increased regulatory oversight through registration and reporting requirements.

Fund managers have responded to investor demands and government regulations by developing extensive operational risk management processes and controls, including systems that are designed to address cybersecurity risks and ensure continuity of business operations, and are also more sensitive to risks associated with the activities of counterparties.

While hedge funds did not pose a risk to financial stability when the financial crisis hit and do not pose such risk today, the end result of the regulations the industry has implemented have made our markets – and hedge funds – safer and more resilient.

In fact, funds have adapted by helping provide capital to businesses and local communities as new regulations have limited banks' lending capabilities.

MFA supports policymakers' efforts to collect the information necessary to provide effective, smart oversight of markets and will continue to work with regulators to implement policies that address systemic risk holistically.

The U.S. financial markets do not operate in a vacuum. As economies function on a global scale, policymakers and regulators must pay careful attention to the impact implementing or changing regulations will have globally. This new, global economy requires harmonization among regulatory regimes, especially those governing U.S. and EU financial markets.

MFA and its members work across geopolitical boundaries and will continue to advocate for liquid, transparent and well-functioning global markets that benefit all investors.

## VIII. ADDENDUM: CALENDAR OF KEY EVENTS

### Major Actions During the First Five Years of Dodd-Frank Act Implementation

2010

#### JULY 21

- The Dodd-Frank Wall Street Reform and Consumer Protection Act is signed into law by President Barack Obama.

2011

#### JANUARY

- The SEC adopted final rules implementing Section 943, requiring nationally recognized statistical rating organizations and issuers of asset-backed securities to provide certain disclosures on the use of representations and warranties in the market for asset-backed securities.
- The SEC also adopted rules to implement Section 945, requiring asset-backed securities issuers whose offerings are registered under the Securities Act to conduct a review of the assets underlying those securities and make certain disclosures about those reviews. The SEC also has adopted rules relating to the ongoing reporting of asset-backed issuers under the Exchange Act.
- The SEC adopted rules concerning shareholder approval of executive compensation and “golden parachute” compensation arrangements to implement Section 951 of the Dodd-Frank Act.

#### APRIL

- The Financial Stability Oversight Council published its process for reviewing nonbank financial companies for potential designation in its final rule and interpretive guidance.

#### JUNE

- The SEC adopted rules that require advisers to hedge funds and other private funds to register with the SEC, establish new exemptions from SEC registration and reporting requirements for certain advisers, and reallocate regulatory responsibility for advisers between the SEC and states. In addition, the SEC amended rules to expand disclosure by investment advisers, particularly about the private funds they manage, and revised the Commission’s pay-to-play rule.

#### JULY

- The SEC granted temporary exemptive relief from clearing agency registration under Section 17A(b) of the Exchange Act to entities that perform certain clearing services for security-based swaps. To qualify for the temporary exemption from registration,

market participants were required to provide identifying information to the SEC about their organization and its activities.

#### OCTOBER

- The SEC and CFTC released final rules relating to Form PF. Form PF will enable the Financial Stability Oversight Council to obtain data that will facilitate the monitoring of risk in U.S. financial markets. The frequency and content of the required filing is based on the type and size of the adviser.

2012

#### JANUARY

- The CFTC adopted final rules to implement a framework for the real-time public reporting of swap transaction and pricing data for all swap transactions.

#### JUNE

- The SEC adopted a final rule relating to mandatory clearing of security-based swaps that establish a process for clearing agencies to provide information to the SEC about security-based swaps that the clearing agencies plan to accept for clearing.
- The SEC adopted rules directing the national securities exchanges to adopt certain listing standards related to the compensation committee of a company’s board of directors as well as its compensation advisers, as required by Section 952 of the Dodd-Frank Act. These standards were approved in January 2013.

#### JULY

- The CFTC adopted rules establishing a schedule to phase in compliance with the clearing requirement under a new section of the Commodity Exchange Act (CEA), enacted under Title VII of the Dodd-Frank Act. The compliance schedule is based on the type of market participants entering into a swap subject to the CFTC’s clearing requirement.

#### AUGUST

- The CFTC and the SEC adopted joint final rules and interpretations that define the terms swap, security-based swap, and security-based swap agreement, and that provide for joint regulation of mixed swaps.

#### OCTOBER

- The Fed issued two final rules on stress testing requirements for certain bank holding companies, state member banks, and savings and loan holding companies

for which the Federal Reserve is the primary federal financial regulator. Nonbank financial companies designated by FSOC will also be subject to certain stress testing requirements contained in the rules. These final rules revise portions of proposed stress testing requirements contained in the Board’s proposed rule to implement enhanced prudential standards issued for comment on December 20, 2011. The Federal Reserve coordinated closely with the FDIC and OCC to ensure consistency and comparability.

- The SEC adopted a final rule establishing minimum standards for the operation, governance, and risk management practices of registered clearing agencies, including clearing agencies designated as systemically important.

2013

#### MARCH

- The SEC issued Release No. 34-69013[16] to request information for a cost-benefit analysis to determine the anticipated economic impacts of moving forward with uniform fiduciary standard rulemaking.

#### APRIL

- The Fed issued a final rule that establishes the requirements for determining when a company is “predominantly engaged in financial activities.” The requirements will be used by FSOC when it considers the potential designation of a nonbank financial company for consolidated supervision by the Federal Reserve.

#### JUNE

- The CFTC adopted final rules on core principles and other requirements for swap execution facilities (SEFs). The final rules implement the SEF registration requirements and establish the execution methods for swaps that are subject to the CFTC’s trade execution requirement.
- The CFTC adopted rules on the process for a designated contract market or SEF to make a swap “available to trade,” and thus subject to the CFTC’s trade execution requirement under the CEA. The rules also establish a schedule to phase in the CFTC’s trade execution requirement.

## AUGUST

- The Fed issued a final rule establishing annual assessment fees for its supervision and regulation of large financial companies. The rule is applicable to companies with \$50 billion or more in total consolidated assets and nonbank financial companies designated by the Financial Stability Oversight Council for supervision by the Federal Reserve.

## SEPTEMBER

- The Fed issued two interim final rules to clarify application of Basel III regulatory capital reforms into capital and business projections for company-conducted stress tests for banking organizations with \$50 billion or more in total consolidated assets and to provide a one-year transition period when conducting initial company-run stress tests for most banking organizations with total consolidated assets between \$10 billion and \$50 billion.

## DECEMBER

- The Fed, CFTC, FDIC, OCC, and SEC, issued final rules to prohibit insured depository institutions and companies affiliated with insured depository institutions from engaging in short-term proprietary trading of certain securities, derivatives, commodity futures and options on these instruments, for their own account (known as the “Volcker rule”). The final rules also impose limits on banking entities’ investments in, and other relationships with, hedge funds or private equity funds.
- The Fed issued a final rule clarifying the treatment of uninsured U.S. branches and agencies of foreign banks, commonly known as the swaps push out provision, which adopts without change an interim final rule issued on June 5, 2013.

2014

## JANUARY

- The CFTC adopted a final rule addressing prohibitions and restrictions on the ability of a banking entity and nonbank financial company supervised by the Fed to engage in proprietary trading and have certain interests in, or relationships with, a hedge fund or private equity fund.

## FEBRUARY

- The Fed issued a final rule to strengthen supervision and regulation of large U.S. bank holding companies (BHCs) and foreign banking organizations (FBOs). The enhanced prudential standards include liquidity, risk management, and capital.

- The CFTC announced the deemed certification of the first “Made Available-to-Trade” (MAT) determination of a SEF for certain fixed-to-floating rate swaps.

## MARCH

- The SEC voted to propose rules to enhance the oversight of systemically-important clearing agencies or those that engage in complex transactions, such as security-based swaps.

- The Fed, FDIC and OCC issued final guidance describing supervisory expectations for stress tests conducted by financial companies with total consolidated assets between \$10 billion and \$50 billion.

## MAY

- The Fed issued final rules repealing its Regulation DD (Truth in Savings) and Regulation P (Privacy of Consumer Financial Information), as the Dodd-Frank Act transferred rulemaking authority for these areas to the Consumer Financial Protection Bureau (CFPB) and the CFPB has already issued interim final rules substantially identical to them. The Board also issued a final rule amending provisions of its Regulation V (Fair Credit Reporting) that require financial institutions and creditors to implement identity theft prevention programs.

## SEPTEMBER

- The Fed, FDIC and OCC issued a final rule that creates a standardized minimum liquidity requirement for large and internationally active banking organizations.

## OCTOBER

- The Fed issued a final rule that amends the Regulation HH risk-management standards for FMUs that have been designated as systemically important and to make related revisions to part I of the Federal Reserve Policy on Payment System Risk, which is applicable to financial market infrastructures more generally. Both sets of revisions are based on and generally consistent with the April 2012 Principles for Financial Market Infrastructures developed jointly by international standard-setting bodies.
- The Fed, FDIC, FHFA, HUD, OCC, and SEC issued a final rule requiring sponsors of securitization transactions to retain risk in those transactions.

## NOVEMBER

- The Fed issued a final rule that generally prohibits a financial company from combining with another company if the ratio of the resulting company’s liabilities exceeds 10 percent of the aggregate consolidated liabilities of all financial companies.

2015

## FEBRUARY

- The SEC proposed rules regarding hedging disclosure to implement Section 955 of the Dodd-Frank Act.

## MARCH

- The SEC adopted rules governing the security-based swap data repository registration process, duties, and core principles.
- The SEC adopted final rules in Regulation SBSR that establishes a framework for regulatory reporting and dissemination of security-based swap information, and proposed a phase-in compliance schedule.

## APRIL

- The SEC proposed rules regarding pay for performance disclosure to implement Section 953 of the Dodd-Frank Act.

## JUNE

- Medium-sized financial institutions with total consolidated assets between \$10 billion and \$50 billion are required to release internal stress test results for the first time.





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