

2020, Fourth Quarter

Compliance Newsletter

Because investment management compliance is constantly changing, we prepare this newsletter to summarize the latest rulings, guidance, proposals and more from the most recent quarter.

To speak to a compliance expert on any of these topics, please contact us at info@joot.io.

HEADLINE SUMMARY

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- SEC Adopts Amendments to the Advertising and Solicitor Rules for Advisers
- SEC Adopts Three New Rules for Registered Funds
- SEC Updates Auditor Independence Rules
- SEC Adopts Amendments to Rules for Exempt Offerings
- SEC Adopts Rules to Modernize the Collection of NMS Market Data
- SEC Proposes Exemptions for Finders Assisting with Capital Raising
- SEC Proposes Amendments to Rule 144 and Form 144
- SEC Issues Risk Alert for Supervision of Branch Offices
- SEC Issues Risk Alert for Investment Adviser Compliance Programs
- SEC Issues Risk Alert for Rule 13h-1: Large Trader
- Updated FAQs for Regulation Best Interest and Form CRS

FINRA

- FINRA Board of Governors Approves Rulemaking Changes
- FINRA Retires Classic CRD Filing for Form U4

IRS

- IRS Adopts Rules for PFICs

NFA

- NFA Adopts Changes to 4.13 Exemption Process

DOL

- DOL Adopts Changes to ERISA Proxy Voting Rule
- DOL Adopts Final Rule for Selecting Plan Investments

**** COVID-19 Regulatory Relief ****

The SEC, FINRA, and CFTC continue to maintain temporary relief provisions for some regulatory obligations and guidance due to the pandemic. Key items that are still in place include:

SEC:

- Relief from mailing certain regulatory communications to shareholders who have addresses outside of the United States
- Extended relief from certain notarization requirements and paper format submissions of regulatory documents
- Extended relief from conducting required in-person meetings (such as board meetings)

FINRA:

- Temporary relief for fingerprint requirements
- Offering an online testing service for certain qualification examinations
- Extending the timeframe (enrollment window) for passing certain qualification examinations

CFTC:

- Relief from the on-site annual inspection of branch offices and guaranteed introducing brokers

Each regulator has a website page that provides information on the guidance or temporary relief that has been issued: [SEC Pandemic Information](#) | [FINRA Pandemic Information](#) | [CFTC Pandemic Information](#)

SEC

SEC Adopts Amendments to the Advertising and Solicitor Rules for Advisers

The SEC adopted amendments to the rules governing investment adviser advertisements and payments to solicitors. The amendments create a single rule that covers advertising and solicitation. The new rules are designed to be more principles-based so that they can accommodate the use of technology in advertising (such as social media). The SEC plans to withdraw no-action letters and other guidance regarding the advertising and solicitation rules that the industry has been following for decades. These amendments will necessitate many changes to an adviser's existing advertising and solicitation procedures. Luckily, the SEC is providing an eighteen-month transition period between the effective date of the rule and the compliance date.

For more information: [SEC Final Rule for Advertising and Solicitation](#)

SEC Adopts Three New Rules for Registered Funds

The SEC was very busy this quarter and passed not one, but **three** new rules for registered funds. All three of these rules will require some detailed analysis and time to ensure they are implemented correctly. The registered fund world is going to be very busy over the next 12 - 18 months creating new procedures for these changes.

Fund of Funds Rule

The SEC adopted new rule 12d1-4 under the Investment Company Act of 1940 to help govern fund of fund arrangements. The rule is designed to create a consistent framework for fund of funds to replace the existing approach, which depends on the SEC's exemptive orders and varies based on an acquiring fund's type. Open-end funds, unit investment trusts, closed-end funds (including BDCs), exchange-traded funds and exchange-traded managed funds will all be able to rely on rule 12d1-4 as both acquiring and acquired funds. The SEC is also rescinding Rule 12d1-2 and certain fund of funds exemptive relief, as well as amending Rule 12d1-1.

For more information: [SEC Final Rule for Fund of Funds](#)

Fund Valuation

The SEC adopted new rules 2a-5 and 31a-4 under the Investment Company Act of 1940 to provide a new framework for fund valuation practices. The rule will permit boards, subject to board oversight and certain other conditions, to designate certain parties to perform the fair value determinations. The rule also will require the performance of certain functions to determine in good faith the fair value of a fund's investments and also provides a definition of when market quotations are not readily available. The SEC will rescind certain guidance and letters that have been issued, including Accounting Series Release 113 (ASR 113) and Accounting Series Release 118 (ASR 118).

For more information: [SEC Final Rule for Valuation](#)

Derivatives

The SEC adopted new rule 18f-4 under the Investment Company Act of 1940 to govern a fund's use of derivatives. The rule requires mutual funds (other than money market funds), ETFs, registered closed-end funds, and BDCs to implement a written derivatives risk management program and designate a derivatives risk manager. The rule will limit the amount of a fund's leverage risk but will also provide exceptions for funds that have limited derivatives exposure. Leverage and inverse ETFs that comply with rule 18f-4 can also rely on Rule 6c-11. The SEC will rescind certain guidance and no-action letters covering derivatives, including the 1979 General Statement of Policy (Release 10666).

For more information: [SEC Final Rule for Derivatives](#)

SEC Updates Auditor Independence Rules

The SEC adopted final amendments to certain auditor independence requirements in Rule 2-01 of Regulation S-X. The changes seek to focus the auditor independence rules on relationships and services that are more likely to jeopardize the objectivity and impartiality of auditors. The amendments will amend the definitions of "affiliate of the audit client" and "audit and professional engagement period." It will also add certain student loans and de minimis consumer loans to the categorical exclusions from independence-impairing lending relationships. This is a good example of the SEC amending a rule to eliminate items that are not actually material conflicts.

For more information: [SEC Rule Amendments for Auditor Independence](#)

SEC Adopts Amendments to Rules for Exempt Offerings

What you need to know: The SEC amended rules to simplify and improve certain aspects of the exempt offering framework to promote capital formation while preserving or enhancing important investor protections. The

amendments are designed to increase the offering limits for Regulation A, Regulation Crowdfunding, and Rule 504 offerings, and revise certain individual investment limits. The amendments will also set clear and consistent rules governing certain offering communications, including permitting certain “test-the-waters” and “demo day” activities. These changes are intended to make the capital raising process more effective and efficient to meet evolving market needs.

For more information: [SEC Rule Amendments for Exempt Offerings](#)

SEC Adopts Rules to Modernize the Collection of NMS Market Data

What you need to know: The SEC adopted rules to modernize the infrastructure for the collection, consolidation, and dissemination of NMS market data. The rules update and expand the content of NMS market data and establish a more efficient process for collecting, consolidating, and disseminating the data to the public. The new processes are intended to address changes in technology and create more efficient distribution of market information.

For more information: [SEC Rule Amendments for NMS Market Data](#)

SEC Proposes Exemptions for Finders Assisting with Capital Raising

The SEC proposed a new exemption from broker registration requirements for “finders” who assist issuers with raising capital in private markets from accredited investors. The exemption would permit natural persons to engage in certain limited activities involving accredited investors without registering as brokers. The proposal would create two classes of finders, Tier I and Tier II, and would outline the requirements for each tier.

For more information: [SEC Proposed Amendments for Finders](#)

SEC Proposes Amendments to Rule 144 and Form 144

The SEC proposed changes to amend Rule 144 under the Securities Act of 1933. The proposal would revise the holding period determination for securities acquired upon the conversion or exchange of certain “market-adjustable securities,” which is intended to reduce the risk of unregistered distributions in connection with sales of those securities. The proposal would also make changes to certain filing requirements of Form 144, including mandating electronic filing of the Form.

For more information: [SEC Proposed Amendments for Rule 144](#)

SEC Issues Risk Alert for Supervision of Branch Offices

What you need to know: The SEC issued a risk alert regarding compliance and oversight expectations of advisers that have multiple branch offices. Deficiencies found by the SEC include lack of (or inadequate) compliance procedures for supervision of branch offices and no oversight of processes for custody, advertising, portfolio management, and conflicts of interest. Advisers that have multiple offices should review this alert and create a remote supervision policy that covers the applicable items that are noted.

For more information: [SEC Risk Alert for Branch Offices](#)

SEC Issues Risk Alert for Investment Adviser Compliance Programs

The SEC issued a risk alert regarding the compliance programs of advisers. The alert is a very comprehensive document that covers deficiencies found with advisers' compliance with the requirements of Rule 206(4)-7 of the Investment Advisers Act. The alert notes common issues such as inadequate compliance resources, insufficient authority of CCOs, annual review deficiencies, and maintaining accurate, written procedures. This document is a good resource for any adviser and should be used as a checklist to ensure you have addressed the items that are specific to your compliance program.

For more information: [SEC Risk Alert for Adviser Compliance Programs](#)

SEC Issues Risk Alert for Rule 13h-1: Large Trader

The SEC issued a risk alert regarding the compliance responsibilities of Rule 13h-1, which is applicable to firms that trade large volumes of shares of NMS securities. Common issues noted for advisers include not having procedures in place to identify when a 13H filing is required, not filing in a timely manner, and not notifying broker-dealers of its obligation to file. The SEC also reviewed broker-dealers' compliance with the rule and found issues with filing and recordkeeping requirements. The key take-away is to make sure your firm has a process to identify when you need to file a 13H, and then make sure you follow the requirements.

For more information: [SEC Risk Alert for Rule 13h-1](#)

Updated FAQs for Regulation Best Interest and Form CRS

The SEC hosted a roundtable meeting in October to discuss its recent reviews of advisers' and broker-dealers' compliance with the Regulation Best Interest and Form CRS rules. As a result of those reviews, the SEC released a set of new Frequently Asked Questions covering the disciplinary history section of the Form CRS. Firms should review these FAQs to ensure the Form CRS documents meet the SEC's requirements.

For more information: [SEC FAQs for Form CRS](#)

FINRA

FINRA Board of Governors Approves Rulemaking Changes

FINRA's Board of Governors approved three proposed rule amendments at its meeting in December. The proposed amendments relate to enhancements of the continuing education program, rules regarding security-based swaps, and establishment of a process to appeal staff statutory disqualification determinations. The Board approved filing of the amendments with the SEC, so stay tuned for more details.

For more information: [FINRA Board of Governors](#)

FINRA Retires Classic CRD Filing for Form U4

“Classic” CRD filing capabilities for Form U4 will retire April 5, 2021. Currently, Form U4 filing is currently available in both “new” and “classic” CRD versions. Users can start using the new filing experience now and provide feedback about that experience to FINRA in the interim.

For more information: [FINRA Online Filing Process for U4s](#)

IRS

IRS Adopts Rules for PFICs

The IRS issued final regulations regarding rules of passive foreign investment companies (“PFICs”). The changes provide an updated definition of when a foreign insurance company is treated as a PFIC and how the PFIC rules apply to tiered ownership structures.

For more information: [IRS Amendments for PFIC Rules](#)

NFA

NFA Adopts Changes to 4.13 Exemption Process

The NFA made changes to the process to file the 4.13 exemption notice. The change requires a statutory disqualification attestation to be filed with the exemption. A firm that currently has a 4.13 exemption is not required to complete the statutory disqualification attestation until it completes the annual exemption affirmation process in 2021.

For more information: [NFA Amendments for 4.13 Exemption](#)

DOL

DOL Adopts Changes to ERISA Proxy Voting Rule

The DOL released a final rule on the application of ERISA fiduciary duties to proxy voting. The final rule takes a principles-based approach on how fiduciaries should carry out their duties of the exercise of shareholder rights, including proxy voting, the use of written proxy voting policies and guidelines, and the selection and monitoring of proxy advisory firms.

For more information: [DOL Final Rule for ERISA Proxy Voting Rules](#)

DOL Adopts Final Rule for Selecting Plan Investments

The DOL released a final rule on the factors for selecting plan investments. The rule clarifies that plan fiduciaries must base their investment decisions solely on pecuniary factors, such as an investment's risk and return based on appropriate time horizons consistent with the plan's investment objectives and funding policy.

For more information: [DOL Final Rule for Selecting Plan Investments](#)

About Joot

Joot is a fintech company that provides web-based technology and services to registered investment advisers, broker-dealers, and funds. Joot has over 40 clients around the U.S. who collectively manage over \$33 billion. Joot's clients include retail advisers, institutional managers, private fund managers, and mutual fund advisers.

For more information about us, please visit our website at www.joot.io or contact us at info@joot.io.