Regulatory Insights for Asset Managers, Mutual Funds and Retirement Firms

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RECENT SEC SPEECHES
Proxy Process: Speech by SEC Commissioner Elad Roisman at the ICI’s Mutual Funds and Investment Management Conference

• On March 18, Commissioner Roisman gave his first speech as a Commissioner, focusing on the SEC’s review of the U.S. proxy process. He explained that Chairman Clayton asked him to lead the SEC’s efforts in considering improvements and stressed his belief in the fundamental importance of the proxy process to the U.S. capital markets.

• In his speech, Commissioner Roisman raised a number of issues he is exploring, including:

Asset manager proxy voting practices:
• Whether it is in the best interest of fund shareholders that advisors should vote on all proposals.

• The issues involved with centralizing proxy voting functions within the fund complex.

Role of proxy advisor firms:
• The impact of asset managers’ use of pre-populated votes in electronic proxy cards.

• How asset managers address errors in proxy advisor recommendations and conflicts of interest.

Other proxy process reforms:
• Referring to the November 2018 Proxy Roundtable, Roisman invited additional feedback regarding what the SEC can do to improve the proxy “plumbing,” stating: “For example, I think it is incumbent on all of us to find a way to achieve end-to-end voting confirmation. I am interested in hearing, from all those involved, about short-term and long-term ways to accomplish this and other improvements.”

• Roisman also commented on the thresholds for submission and resubmission of shareholder proposals and invited feedback regarding whether the SEC should raise or modify the current monetary thresholds and holding periods noting: “It is important to achieve a balance here so that we allow for robust shareholder engagement without providing a mechanism for certain shareholders with idiosyncratic views to use the shareholder proposal system in a way that does not benefit the interests of the majority of long-term shareholders.” The full speech can be found at: https://www.sec.gov/news/speech/speech-roisman-031819
Speech by Dalia Blass (Director, Division of Investment Management, SEC) at the ICI's Mutual Funds and Investment Management Conference

• In her speech on March 18, Director Blass discussed the Division of Investment Management’s (“IM”) accomplishments in 2018 and their 2019 agenda:

  – 2018 accomplishments to improve the investor experience included a request for comment on how to improve investment company disclosures, reforms to improve variable annuity disclosure through the use of a summary prospectuses, and the adoption of a notice and access approach to the delivery of shareholder reports (rule 30e-3). She also noted a number of rule proposals, including Regulation Best Interest, the ETF proposal, fund of funds, fund liquidity reporting and fund research reports.

  – Blass also discussed the launch of their Board Outreach Initiative and no-action letters on the affiliated transaction rules, in-person meeting requirements (discussed below) and engagement with boards to update the Commissions’ valuation and auditing guidance.

  – For 2019, Blass discussed next steps for their Investor Experience Initiative, such as exploring options for a summary mutual fund shareholder report, ways to improve fee and risk disclosures and as part of the SEC’s Regulation Best Interest rule making, recommendations on Form CRS and investment advisor’s fiduciary duty interpretation. She also noted that finalizing the ETF and fund of funds rules will be a high priority for IM.

  – Next up for their Board Outreach Initiative, the next anticipated milestone will be recommending updates to the Commission’s valuation guidance. She also noted a proposal for business development company and closed-end fund offering reforms (that was just issued). And she anticipates that IM will present recommendations for a proposal on modernizing the advertising and solicitation rules for investment advisers and a proposal for use of derivatives by investment companies.

  – On MiFID II, Blass raised the 2017 no-action letters and discussed the issues the SEC staff is examining, including the impact to the ‘many parties and interests involved.’ They are also looking at the Advisers Act, which they believe could already provide enough flexibility to accommodate solutions for the industry. And she also said they are looking for market solutions and invited further engagement with the staff.

  – Blass also addressed long-term trends, noting that regulatory changes should only be made with a clear understanding of costs and benefits, including unintended consequences. With this in mind, Blass said IM has a new outreach initiative with small and mid-sized fund sponsors regarding regulatory barriers asking “are there barriers making it harder for small and mid-sized fund sponsors to compete?” She also discussed their plans to form an asset management advisory committee composed of experts with diverse viewpoints to discuss issued facing the asset management industry.

  – Other initiatives include review of previous staff statements and guidance, ways to improve the exemptive applications process, use of proxy advisor firms and international policy.

• Blass’s full speech can be found at: https://www.sec.gov/news/speech/speech-blass-031819

SEC RULEMAKING
Variable Annuity and Variable Life Insurance Summary Prospectus Rule Proposal

• On October 30, the SEC proposed a summary prospectus rule for variable annuities and variable life insurance products. See the March 2019 Regulatory Insight for a detailed summary of the rule proposal: https://www.broadridge.com/_assets/pdf/broadridge-asset-management-regulatory-insights-march-2019.pdf

• The Release can be found at: https://www.sec.gov/rules/proposed/2018/33-10569.pdf

• Industry comment letters, including a letter submitted by Broadridge can be found at: https://www.sec.gov/comments/s7-23-18/s72318.htm
SEC Rule Proposal: Securities Offering Reform for Closed-End Investment Companies

• As directed by Congress through two 2018 laws, The Small Business Credit Availability Act and The Economic Growth, Regulatory Relief, and Consumer Protection Act, the SEC proposed rules that would modify the registration, communications, and offering processes for business development companies (“BDCs”) and registered closed-end investment companies (“CEFs” and together “affected funds”). The stated goals of these modifications is “to allow these investment companies to use the securities offering rules that are already available to operating companies.”

• Comment Period: 60 day comment period after publication in Federal Register

• The rule proposal can be found at: https://www.sec.gov/rules/proposed/2019/33-10619.pdf

FAST Act Modernization and Simplification of Regulation S-K

• On March 20, the SEC adopted amendments to modernize and simplify disclosure requirements in Regulation S-K for operating companies. For consistency, the release contains certain parallel amendments for investment companies:
  
  – Incorporation by Reference and html. Funds will no longer be required to file documents (and amendments) that are incorporated by reference in a filing. Instead, funds will be required to file reports and registration statements in html format and include links if the documents are available on EDGAR. Effective April 1, 2020.

  – Non-functioning or Incorrect Hyperlinks. For effective registration statements and reports on Form N-CSR, registrants may correct inaccurate or nonfunctioning links in the next post-effective amendment, or next report on Form N-CSR. For registration statements not yet effective, an amendment is required to be filed. Effective April 1, 2020.

  – Redaction of Confidential Information. Effective April 2, 2019, funds are allowed to redact certain information from exhibits filed as “other material contracts,” without filing a confidential treatment request. The information must be not material, and would likely cause competitive harm to the registrant if publicly disclosed.

• For additional details, the final rule and adopting release can be found at: https://www.sec.gov/rules/final/2019/33-10618.pdf

RETIREMENT

Retirement Bills in Congress

• A Senate retirement bill, the Retirement Enhanced Savings Act (“RESA”) was re-introduced the first week of April and a House bill, Setting Every Community Up For Retirement Enhancement (“SECURE”) Act of 2019 was voted out of committee; both bills have bipartisan support and there is widespread agreement that these bills could be enacted in 2019.

• Many of the same provisions in prior retirement bills were included, such as Open Multi Employer Plans (“MEPs”), repeal of the age cap for contributions to Traditional IRAs, advancing lifetime income solutions, increasing the 10% limit on automatic escalation to 15% and increasing required minimum distributions to age 72 (from in age 70 ½).

• The Senate bill can be found at: https://www.finance.senate.gov/imo/media/doc/OTT19202%20(002)%20As%20filed.pdf

• On overview of the House bill can be found at: https://waysandmeans.house.gov/sites/democrats.waysandmeans.house.gov/files/documents/SECURE%20Act%20section%20by%20section.pdf

OTHER GUIDANCE AND NEWS

SEC No Action Relief - Relaxes In-Person Voting Board Requirements

• On February 28, the Staff of the Division of Investment Management issued a no-action letter to the Independent Directors Council. Under the conditions stipulated in the request, the no-action letter allows fund boards of directors greater flexibility in complying with the “in-person” voting requirements under the Investment Company Act of 1940 for certain approvals, including the approvals and renewals of investment advisory contracts, approvals of the fund’s independent public accountants and renewal of Rule 12b-1 plans. See the letter for more details.
• The no-action letter applies in two circumstances:

– The directors needed for the required approval cannot meet in person due to unforeseen or emergency circumstances, provided that (1) no material changes to the relevant contract, plan and/or arrangement are proposed to be approved, or approved, at the meeting, and (2) such directors ratify the applicable approval at the next in-person board meeting; and

– The directors needed for the required approval previously fully discussed and considered all material aspects of the proposed matter at an in-person meeting but did not vote on the matter at that time, provided that no director requests another in-person meeting.

• The no-action letter can be found at: https://www.sec.gov/divisions/investment/noaction/2019/independent-directors-council-022819

SEC: Expected Commission Changes

• It was widely reported that Commissioner Robert Jackson will step down by the Fall and return to New York University Law School. Although his term could extend until 2020, it is expected that he will begin teaching in the Fall semester.

• Separately, President Trump announced his intention to nominate Allison Lee to fill the open Democratic seat on the U.S. Securities and Exchange Commission.

• The selection of Lee to replace Kara Stein, who left the SEC in January after her term ended, would effectively fill her seat but leaving one open Democratic position due to Jackson’s expected departure. Lee is a former aide to Stein who also worked as an enforcement division lawyer during her time at the agency.

Final SEC Rule 30e-3 – Optional Internet Availability of Investment Company Shareholder Reports

• Rule 30e-3 will allow mutual funds to send a notice of internet availability instead of a shareholder report, effective January 1, 2021, to reduce printing and postage costs. Funds intending to rely on the rule in 2021 must disclose this change in their shareholder reports and prospectuses beginning this year (2019). Investors have the right to opt-out and continue to receive full paper reports (as they do today).

• Broadridge now offers a comprehensive solution that captures investor distribution preferences through a centralized website FundReports and, is working with banks, brokers and mutual funds, to permits easier enrollment in e-delivery. Use of unique control numbers and QR codes simplifies the election process for shareholders (including via mobile device) by routing them directly to the website.

• On August 3, Twin River Paper Company, Consumer Action, the Paper Coalition and other entities filed suit in DC Court of Appeals to prevent the SEC from implementing the final rule. Both parties filed written briefs with the court and oral arguments took place on March 12.

SEC Release on NYSE Interim Fees

• Broadridge and other industry comment letters were filed on October 31, 2018. The SEC staff continues to digest comments and meet with industry groups on its Request for Comments.

• The Release and comment letters can be found at: https://www.sec.gov/comments/s7-13-18/s71318.htm#meetings

Proposed Regulation Best Interest and Form CRS

• The SEC’s Fall Reg Flex agenda lists September 2019 for final rulemaking and in a March 26, 2019 speech at SIFMA’s Compliance and Legal Society conference, Chairman Clayton noted that Regulation Best Interest is on his list of strategic initiatives for 2019.

• At the SIFMA conference, Robert Colby, FINRA’s chief legal officer, said FINRA may retract their suitability rule once the SEC approves Regulation Best Interest. Once the rule is final, he said that FINRA will review it and work to “fix” potential differences and inconsistencies, “We’ll also look to see if there’s any reason for us to continue to have a separate suitability rule, because we’ll be enforcing Reg B.”

• Brett Redfearn, the Director of the SEC’s Division of Trading and Markets said at the conference that they are working with state authorities to reduce discrepancies between various proposed conduct standards and the federal rule. Further he said they are still reviewing comment letters “but hopefully we’re wrapping up.”

• The SEC’s press release, rule proposals and industry comment letters can be found at: https://www.sec.gov/news/press-release/2018-68
HR 1815 - SEC Disclosure Effectiveness Testing Act

• On March 18, 2019, HR 1815 was introduced by Representative Casten (D-IL-6). The bill would require the SEC to conduct investor testing of retail disclosures prior to rules being issued (including a respective review of existing disclosures), such as the proposed disclosures required by Regulation Best Interest. It would also require the SEC to provide annual reporting to Congress on the status and results of such investor testing.

• The draft bill can be found at: https://financialservices.house.gov/uploadedfiles/bills-116-hr1815-c001117-amdt-1.pdf

Staff Bulletin on 485(a) Filings and New SEC Fund Disclosure Website

• On April 2, IM announced its latest Accounting and Disclosure Information (“ADI”) - 2019-07 – Review of Certain Filings Under Automatic Effectiveness Rules. The ADI explains how funds should work with the SEC to streamline the use of rule 485(a) for automatic effective filings.

• The Staff Bulletin can be found at: https://www.sec.gov/investment/accounting-and-disclosure-information/adi-2019-07-review-certain-filings-under-automatic

• The Division of Investment Management’s Disclosure Review and Accounting Office (DRAO) created a fund disclosure section on IM’s website, which includes its responsibilities, a central place to see existing guidance and other disclosure resources. The new information can be found at: https://www.sec.gov/investment/fund-disclosure-at-a-glance

SEC Issues Digital Assets Framework

• On April 3, the SEC provided guidance to help those seeking to comply with the U.S. federal securities laws, stating: “The framework is not intended to be an exhaustive overview of the law, but rather, an analytical tool to help market participants assess whether the federal securities laws apply to the offer, sale, or resale of a particular digital asset.”

• The SEC’s Statement and Framework can be found at: https://www.sec.gov/news/public-statement/statement-framework-investment-contract-analysis-digital-assets

• The SEC issued a no-action letter on April 3 to TurnKey Jet, Inc., allowing a digital asset not to register under the terms of the no-action letter. The letter can be found at: https://www.sec.gov/divisions/corpfin/cf-noaction/2019/turnkey-jet-040219-2a1.htm

• More information about digital assets can be found at the SEC’s Strategic Hub for Innovation and Financial Technology (“FinHub”): https://www.sec.gov/finhub

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