

# Your Quarterly Regulatory Briefing\*

(compliments of Daphne Chisolm and Cyndie Baughman)



*The SEC issues several no-action letters, study says chief compliance officer pay may be going up, and the SEC gets a new commissioner . . . This is Your Quarterly Briefing.*

**October 1, 2018**

## Industry Regulatory & Enforcement Activity

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## Education & Training

This section lists upcoming conferences as well as on-line learning opportunities and free webinars suitable for various parties – trustees, compliance professionals, or those seeking CPE or CLE credits.

## Industry Observations

This section provides a brief update on trends.

## Filing Tips

This section provides some helpful hints on keeping up with EDGAR filings.

\* *For the Quarter Ended September 30<sup>th</sup>.*

*About the Authors: Daphne Chisolm and Cyndie Baughman are attorneys that each have over 20 years of experience in the financial services and investment management industry. Ms. Chisolm has particular expertise in the area of exchange-traded funds. Ms. Baughman and Ms. Chisolm have been colleagues for nearly their entire careers and worked together at Dechert, LLP in Washington D.C. The Authors thank Nanlee Vang, who has extensive experience and proficiency in Workiva, a cloud-based EDGAR filing platform, for her contributions to this Quarter's Briefing.*

## **INDUSTRY REGULATORY & ENFORCEMENT ACTIVITY**

### **1. SEC Charges an Adviser and its CEO with Misleading Investors**

On July 18, 2018, the Securities and Exchange Commission (the “SEC”) announced that it charged Temenos Advisory, Inc., a Connecticut-based investment advisory firm, and George L. Taylor, its chief executive officer, with putting \$19 million of investor money, including elderly investors, in risky investments and taking large commissions from those investments. In its complaint, the SEC alleges that Temenos Advisory, Inc. steered investor dollars into risky and illiquid private offerings and concealed from these clients the high commissions taken by the firm. Read the full Press Release [here](#).

### **2. SEC Appoints New Deputy Director of OCIE**

On July 25, 2018, the SEC announced that Kristen Snyder has been named Deputy Director of the Office of Compliance Inspections and Examinations (“OCIE”). Ms. Snyder will replace Jane Jarcho who retired at the end of August. Ms. Snyder has been with the SEC for 15 years and has served in multiple roles. Ms. Jarcho was a career SEC employee giving 28 years to the agency.

### **3. SEC Updates List of Firms Using Inaccurate Information**

On August 6, 2018, the SEC announced it updated its currently running list of unregistered firms that use misleading information to target and solicit non-U.S. investors. Typically, the list includes firms that claim to be registered and are not, firms that impersonate legitimate firms, and fake regulators. This list is based on firms subject to investor complaints and is known as “Public Alert: Unregistered Soliciting Entities” or “PAUSE.” The list can be found [here](#).

### **4. The Division of Investment Management Issues Several No-Action Letters During the Quarter**

On August 7, 2018, the Division issued a response to a request for no-action from Charles Schwab & Co., Inc. on Section 206(4) and Rule 206(4)-3 of the Investment Advisers Act of 1940 on cash payments for solicitation of advisory clients and on July 20, 2018, the Division issued a response to a request for no-action in regard to Rule 14a-8 under the Securities Exchange Act of 1934 relating to informal procedures on shareholder proposals. If you are following these developments, the Section 206 no-action letter can be found [here](#) and the Rule 14a-8 no-action letter can be found [here](#).

On September 13, 2018, the SEC issued a response to a request for no-action in regard to two closed-end PIMCO Funds (*PIMCO Corporate & Income Opportunity Fund* and *PIMCO Income Opportunity Fund*) and their use of Rule 486(b) under the Securities Act to file post effective amendments to their registration statements. The SEC agreed to PIMCO’s request to use Rule 486(b) in the limited circumstances it proposed in regard to amending an equity shelf registration statement so it would become effective immediately. The incoming letter and the Staff’s no-action letter issued by the SEC can be found [here](#).

### **5. CCO’s May Have Seen Pay Increases from 2016 to 2017 According to MPI Survey**

In a publicly available [webinar](#), Management Practice, Inc. (“MPI”) released information on its 2017 survey of chief compliance officer compensation (the “Survey”). The Survey found an increase in compensation since its similar survey conducted in 2016. The Survey also noted that in firms interviewed the salary range in 2017 for the chief compliance officer position was \$100,000 to \$1 million and the average total compensation from those surveyed was \$431,957, up from \$403,375 in 2016. The Survey also noted trends such as receipt of bonuses, bonuses tied to company performance, retirement plan information, experience backgrounds of chief compliance officers, employee benefits such as 401k, and

whether salaries were paid by the funds or other entities. MPI has conducted this type of survey since 2006 and for the 2017 survey it noted that it had 60 participants.

## **6. Office of Investor Education Issues Alert on the Topic of Self-Directed IRAs**

On August 8, 2018, the Office of Investor Education (the “Office”) issued an investor alert titled [“Self-Directed IRAs and the Risk of Fraud.”](#) In the alert, the Office notes that self-directed IRAs allow investment in a broader portfolio of assets which could make them riskier. The alert discusses certain fraud risks and how investors can work to mitigate those risks for themselves by asking certain questions, avoiding certain investment offers, and looking for specific items that may raise red flags as well as discusses actions the SEC has taken to combat fraud in this space.

## **7. SEC Charges Citigroup for Books and Records Violations**

On August 16, 2018, the SEC announced that Citigroup had agreed, in response to charges brought, to settle two enforcement actions involving books and records violations, internal accounting controls, and trader supervision. The actions related to \$81 million in losses due to trader mismarking and unauthorized proprietary trading as well as \$475 million in losses due to fraudulently-induced loans. Citigroup agreed to pay more than \$10 million for the violations. Mark P. Berger, Director of the SEC’s New York Regional Office stated that “Citigroup’s lax supervision and weak internal controls allowed a handful of rogue traders to mismark positions over several years and, separately, resulted in the unnecessary loss of hundreds of millions of dollars of its shareholders’ assets to fraud.” Read the full Press Release [here](#).

## **8. SEC Adopts Amendments to Simplify and Update Disclosures**

On August 17, 2018, the SEC announced it would adopt amendments to certain disclosures that have become duplicative, overlapping and outdated in light of other disclosures. A fact sheet on the amendments can be found [here](#) and the final rule may be found [here](#). The amendments became effective 30 days after publication in the Federal register. The amendments relate primarily to public reporting companies; however, some also relate to investment companies and investment advisers.

## **9. Associate Director Barry Miller Leaves the SEC**

The SEC announced on August 23, 2018 that Barry D. Miller, Associate Director of Disclosure Review and Accounting in the Division, will retire at the end of August after 40 years of public service, including over 30 at the SEC.

## **10. Fee Rate Advisory for Next Year**

The SEC announced on August 24, 2018 that fees that public companies and other issuers pay to register their securities with the SEC will be \$121.20 per million dollars in fiscal year 2019. The current filing fee rate is \$124.50. Investment companies filing Form 24F-2NT should ensure to update the fee multiplier under Item 5(vii) for filings after October 1, 2018.

## **11. SEC Whistleblower Award**

On September 6, 2018, the SEC awarded more than \$54 million to two whistleblowers who provided critical information and continued assistance to the Staff helping it bring an enforcement action. Of the \$54 million, \$39 million was awarded to one whistleblower and \$15 million to another - \$39 million being the second largest award since the inception of the whistleblower program. Jane Norberg, Chief of the SEC’s Office of the Whistleblower, stated that “[w]histleblowers serve as invaluable sources of information, and can propel an investigation forward by helping us overcome obstacles and delays in

investigation ... These substantial awards send a strong message about the SEC's commitment to whistleblowers and the value they bring to the agency's mission."

## **12. New SEC Commissioner Sworn in on September 11, 2018**

Elad Roisman was sworn in as an SEC Commissioner on September 11, 2018. Mr. Roisman previously served as counsel to SEC Commissioner Daniel Gallagher and was in private practice. Mr. Roisman will fill a term that expires on June 5, 2023. The Press Release may be found [here](#).

## **13. Division of Investment Management Announces Acting Associate Director**

On September 19, 2018, the Division announced that Jennifer B. McHugh had been named as Acting Associate Director of the Disclosure Review and Accounting Office, replacing Barry Miller who recently retired. Ms. McHugh served in various roles at the SEC including as Senior Advisor to SEC Chairpersons Mary L. Schapiro and Mary Jo White as well as in the private sector as an associate at Dechert LLP. The announcement can be found [here](#).

## **14. SEC's Enforcement Program – Speech**

On September 20, 2018, Stephanie Avakian, Co-Director of the SEC's Enforcement Division, gave a speech in Dallas, Texas on the topic of "Measuring the Impact of the SEC's Enforcement Program." A transcription of the speech can be found on the SEC's website [here](#).

Ms. Avakian noted that she felt the Enforcement Division had a strong year and she highlighted certain cases brought. She also covered topics such as (i) misconduct in the ICO (initial coin offering) and digital asset space; (ii) the SEC's share class disclosure initiative; and (iii) certain challenges faced by the SEC including external challenges such as Supreme Court decisions as well as internal challenges such as numerous personnel changes and significant vacancies in senior leadership.

## **15. SEC and NYU Host Forum on High-Frequency Trading and Liquidity Resiliency**

On September 21, 2018, the SEC's Division of Economic and Risk Analysis and Division of Trading and Markets partnered with New York University's Salomon Center for the Study of Financial Institutions to host a forum on high-frequency trading and liquidity resiliency. The program was geared toward regulators, practitioners and academics and was held at the SEC's headquarters in Washington, D.C.

The three substantive panels in the program were moderated by SEC representatives including recently sworn-in Commissioner Roisman and included: (i) regulation, HFT, and the need for speed; (ii) market making, automation, and the potential for disruptive trading; and (iii) the evolution of liquidity provision and liquidity resiliency.

The webcast of the program will be made available in the future [here](#).

## **16. SEC Charges Firm with Inadequate Cybersecurity Procedures**

On September 26, 2018, the SEC announced that it had charged Des Moines-based broker-dealer and investment adviser Voya Financial Advisors Inc. ("Voya"). Voya agreed to pay \$1 million to settle charges brought against it relating to violating the Safeguards Rule and the Identity Theft Red Flags Rule which resulted in failures in cybersecurity policies and procedures resulting in an intrusion that compromised thousands of customers' personal information.

According to the SEC’s order, cyber intruders impersonated Voya contractors by calling Voya’s support line and requesting contractor passwords be re-set. This allowed the intruders to use the new passwords to gain access to over 5,000 customer accounts.

The Voya settlement is the first obtained by the SEC relating to violations of the Identity Theft Red Flags Rule. More details can be found on the SEC’s website [here](#).

**17. Proxy Process Roundtable to be Hosted by the SEC**

The SEC will host a proxy process roundtable at its Washington D.C. headquarters on November 15, 2018. The focus of the roundtable is to hear from investors, issuers and other market participants about their views on the proxy rules and process generally. The SEC is accepting electronic and paper submissions on the proxy process at the below addresses and with the following reference identifier:

- (i) e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov)
- (ii) mail to Brent Fields, Secretary, SEC, 100 F. Street, N.E., Washington, D.C. 20549-1090
- (iii) refer to File Number 4-725

**18. Division of Investment Management Issues Money Market Statistics Report**

On September 26, 2018, the Division of Investment Management’s Analytics Office issued a report titled “Money Market Statistics” which can found [here](#) on the Division’s web page. The data in the report is as of August 31, 2018 and contains 17 pages of data including showing downward trends in the asset levels and funds in this space.

**19. IM Information Update on Staff Proxy Advisory Letters**

The Division of Investment Management issued [IM-INFO-2018-02](#) on the topic of Staff proxy advisory letters. The Staff noted the upcoming Roundtable (*discussed in 17. above*) and stated that it is working on developing an agenda for the Roundtable which may include topics such as advisers’ responsibilities in voting client proxies and the use of proxy advisory firms. The Staff reminded the industry that Staff guidance is non-binding. The Staff noted that it had determined in advance of the Roundtable to rescind two previously issued letters (i) the 2004 Egan-Jones Proxy Services letter; and (ii) the 2004 Institutional Shareholder Services, Inc. letter. The Staff noted that it re-examined these letters and determined to rescind them as it hopes it would facilitate the Roundtable’s discussion.

*The above is merely our summary of industry activities that we feel may be of the most interest to those in the investment management field – funds, their trustees/directors and service providers. The full text of SEC press releases, proposed and adopted rules, enforcement actions and other news can be found on the [SEC’s Website](#).*

**EDUCATION & TRAINING**

Date	Location	Sponsor	Event
Various	On-Line	Financial Industry Regulatory Authority (“FINRA”)	FINRA offers a variety of e-learning courses, free webinars, and other events that can be found <a href="#">HERE</a> .
September 30 – October 3, 2018	San Diego, California	Investment Company Institute (“ICI”)	2018 Tax and Accounting Conference
October 1, 2018	Washington, D.C.	Securities Industry and Financial Markets Association	SIFMA Annual Meeting
October 9, 2018	New York, New York	FINRA	2018 FINRA Disclosure Reporting, Monitoring and Registration

			Conference
October 15, 2018	Chicago, Illinois	Independent Directors Council (“IDC”)	2018 Fund Directors Conference
October 25, 2018	Washington, D.C.	ICI	2018 Securities Law Development Conference
November 7, 2018	Santa Monica, California	FINRA	2018 Small Firm Conference
November 14, 2018	New York, New York	ICI	2018 Closed-End Fund Conference
March 17-20, 2019	San Diego, California	ICI	2019 Mutual Funds and Investment Management Conference
May 15-17, 2019	Washington, D.C.	FINRA	2019 Annual Conference

## **INDUSTRY OBSERVATIONS**

*ETF Rule Proposal.* The comment period for the ETF rule proposal ended October 1, 2018. To date, commentators generally are supportive of a new rule, but have questioned some of the rule's proposed requirements. Specifically, whether it makes sense to require every ETF sponsor to provide and maintain an interactive calculator on its website to facilitate comparison of trading cost impact if methodology calculations are likely to vary across fund groups. Also, commentators point to the rule's omission of fund-of-fund relief, which has been routinely granted in past ETF exemptive orders. They note that new ETF sponsors may be unwilling to launch new products without this relief and, as a consequence, would need to file for fund-of-fund exemptive relief even if the ETF rule proposal is adopted.

*Affiliated Index Providers.* The SEC staff continues to focus and gather information on ETFs that utilize affiliated or custom indexes. New rule proposals addressing the SEC's thoughts in this area may be forthcoming.

*Clean Shares & Free Shares* – Even though the Department of Labor’s fiduciary rule may have gone away, “clean shares” (those only charging management fees) seem to be here to stay. Taking it a step beyond clean shares to “free shares” is Fidelity with four new index fund products that charge nothing. See Fidelity ZERO Large Cap Index Fund and Fidelity ZERO Extended Market Index Fund which became effective mid-September within its Fidelity Concord Street Trust and Fidelity ZERO International Index and Fidelity ZERO Total Market Index within its Fidelity Salem Street Trust which, as of the date of this newsletter, are not yet effective. An article in *Bloomberg* discussing these funds can be found [HERE](#).

*Cryptocurrency & Fund Innovations* – For those following these products, the Division of Investment Management has a useful [link](#) that includes the Staff’s January 18, 2018 letter to the Investment Company Institute (“ICI”) and Securities Industry and Financial Markets Association (“SIFMA”) and public submissions on the topic as recent as September 19, 2018. Recall that the January 18, 2018 letter authored by Dalia Blass, the Division Director, stated to the ICI and SIFMA that the Division would consider certain questions relating to these products such as liquidity, custody, and valuation and would “table” registration statements for funds investing substantially in cryptocurrency and related products.<sup>1</sup>

<sup>1</sup> Specifically, Ms. Blass’ letter indicates:

Until the questions identified above can be addressed satisfactorily, we do not believe that it is appropriate for fund sponsors to initiate registration of funds that intend to invest substantially in cryptocurrency and related products, and we have asked sponsors that have registration statements filed for such products to

## **FILING TIPS**

As noted in Item 10 above the fee rate advisory for the next fiscal year beginning on October 1, 2018 has been reduced so relevant EDGAR forms should be adjusted accordingly.

As the regulatory filing season heats up, now is the time to get organized. Prepare a time and responsibility table identifying the parties responsible for review of annual reports and registration statements. Remember to set deadlines and take into account everyone's vacation schedules for the remainder of the year. A format for your table could look like this:

<b><u>Date</u></b>	<b><u>Action</u></b>	<b><u>Responsible Party</u></b>
October 1, 2018	<b>First Full Distribution</b> of prospectus and statement of additional information for review	Legal
October 10, 2018	<b>Comments due on First Full Distribution</b>	Compliance Product Development Sales

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withdraw them. In addition, we do not believe that such funds should utilize rule 485(a) under the Securities Act, which allows post-effective amendments to previously effective registration statements for registration of a new series to go effective automatically. If a sponsor were to file a post-effective amendment under rule 485(a) to register a fund that invests substantially in cryptocurrency or related products, we would view that action unfavorably and would consider actions necessary or appropriate to protect Main Street investors, including recommending a stop order to the Commission.