Issue 20, August 2014

REGULATORY ADMINISTRATION DIGEST

The following is a summary of select developments in investment management regulation during the second quarter of 2014.

TOPICS IN THIS ISSUE:

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REGULATORY AND ENFORCEMENT DEVELOPMENTS

MONEY MARKET FUND REFORMS ADOPTED

On July 23, 2014, the Securities and Exchange Commission (the "SEC") adopted a Final Rule that includes several amendments to the rules governing money market funds. The amendments provide that:

- Prime institutional money market funds must use a "floating," market-based net asset value ("NAV") rounded to the fourth decimal place, in place of the $1.00 per share stable NAV that money market funds currently use;
- Boards of non-government (institutional or retail) money market funds may impose liquidity fees of up to 2% on investor redemptions and/or suspend redemptions in certain circumstances ("gate"); and
- All money market funds will be subject to additional stress-testing and disclosure requirements, including: daily disclosures on mutual funds' websites (NAV per share, daily and weekly liquid assets levels, net shareholder flows, use of affiliate or sponsor support, and imposition of fees and gates); prompt disclosure on new Form N-CR of material events (imposition or removal of fees or gates, portfolio security defaults, affiliate or sponsor supports, and, for certain funds, a fall of NAV per share below $0.9975); and disclosure in a money market fund's Statement of Additional Information of any affiliate or sponsor report during the last 10 years.

The SEC intends these long-anticipated changes to decrease the susceptibility of money market funds to large-scale redemptions, such as those seen during the 2008 onset of the financial crisis, and to increase the ability of investors to obtain information about risks associated with such funds.

The reforms also include additional diversification requirements and re-propose other amendments to Rule 2a-7 under the Investment Company Act of 1940 (the "1940 Act"), including the removal of references to credit ratings. The reforms

include corresponding changes to Form PF, under the Investment Advisers Act of 1940, for unregistered liquidity funds. Also, the IRS is expected to issue guidance to address the tax consequences for investors in money market funds subject to the new floating NAV requirement.

The compliance date for the floating NAV and liquidity fee/gate reforms is two years after the publication of the Final Rule in the Federal Register. The other reforms will have shorter compliance dates between nine and 18 months from publication.

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WHISTLEBLOWER AWARD ANNOUNCED

On June 3, 2014, the SEC announced that whistleblower award exceeding $875,000 would be split evenly between two individuals who provided tips and assistance to help the agency bring an enforcement action. In a press release, the SEC stated that the "whistleblowers provided original information and assistance that enabled [the SEC] to investigate and bring a successful enforcement action in a complex area of the securities market. The press release also stated that the SEC's whistleblower program had awarded a total of eight whistleblowers since it began in late 2011.

ADVISER CHARGED WITH IMPROPER CALCULATION OF FEES AND OVERCHARGING CLIENTS

On April 3, 2014, the SEC announced charges against a St. Petersburg, Florida-based financial services firm, Transamerica Financial Advisers ("Transamerica"), for improperly calculating advisory fees and overcharging clients. The SEC alleged that the firm failed to process requests by clients to aggregate accounts in order to qualify for fee discounts and had conflicting policies on whether representatives were required to pass on to clients the savings from breakpoint discounts. The SEC alleged that, because of these lapses, Transamerica overcharged certain clients by failing to apply applicable discounts. In addition, the SEC alleged that Transamerica failed to have adequate policies and procedures to ensure that it was properly calculating its fees.

The SEC found that the Transamerica willfully violated Sections 206(2), 206(4), and 207 of the Investment Advisers Act of 1940 (the "Advisers Act") and Rule 206(4)-7 under the Advisers Act. Without admitting or denying the SEC's findings, Transamerica agreed to settle the SEC's charges and reimbursed 2,304 current and former client accounts with refunds and credits totaling $553,624, including interest. Transamerica also agreed to pay an additional $553,624 penalty and to a censure.

SEC GUIDANCE AND INITIATIVES

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IM Staff Issues New Guidance

Proxy Voting. On June 30, 2014, the SEC's Divisions of Investment Management (the "IM Division") and Corporate Finance released *Staff Legal Bulletin No. 20* ("Bulletin") to provide adviser's guidance on their responsibilities in voting client proxies and retaining proxy advisory firms. Through a series of questions and answers, the Bulletin covers a range of topics related to proxy voting, including proxy voting procedures, delegation of proxy voting, and the role and oversight of proxy advisory firms.

Mutual Fund Disclosure. In *IM Guidance Update No. 2014-08*, the IM Staff discusses ways to enhance the disclosures required to be included in the summary section of mutual fund statutory prospectuses. As an initial matter, the IM Staff stated that it had observed a significant number of prospectuses in which disclosure remains complex, technical and duplicative and that a significant number of summary sections were unnecessarily long. The Guidance Update focuses on select rules and form requirements that IM Staff have commented on in connection with its review of mutual fund registration statements. Specific guidance provided includes reminders to:

- Summarize the principal investment strategies and risks;
- Include only required or permitted information in the summary section;
- Include non-principal strategies and risks in the statutory prospectus; and
- Avoid cross-references and use plain English.

Affiliated Transactions. In *IM Guidance Update 2014-06*, the IM Staff reminds mutual funds that are series companies about the importance of ensuring that their compliance policies and procedures are reasonably designed to prevent violations of the federal securities laws as they apply to each series. Among other things, the IM Staff stated that a fund should review its compliance policies and procedures for the appropriate identification of "affiliated persons" with respect to each series of the mutual fund for purposes of transactions that may be prohibited under the 1940 Act.

Deregistration Applications on Form N-8F. In *IM Guidance Update 2014-05*, the IM Staff provides guidance on avoiding commonly observed deficiencies in deregistration applications on Form N-8F. The IM Staff's comments cover Items 2 (fund name), 6 (applicant contact person), 11 (identity of adviser(s)/subadviser(s), 15(a) (board approval) and 25 (current fund activities) of Form N-8F and the verification found at the end of Form N-8F.

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HIGHLIGHTS FROM RECENT SEC SPEECHES

SEC Chair White on the Role of Directors. On June 23, 2014, in a speech titled *A Few Things Directors Should Know About the SEC*, SEC Chair Mary Jo White discussed the role of directors as gatekeepers for shareholders. Among other things, she that the SEC typically use the term "gatekeeper" to refer to those "who have professional obligations to spot and prevent potential misconduct" and that "directors serve as [the] most important gatekeepers. For by law, it is ultimately the fiduciary responsibility of the board of directors to oversee the business and affairs of a company." She further stated that "[i]n discharging this important responsibility, it is essential for directors to establish expectations for senior management and the company as a whole, and exercise appropriate oversight to ensure that those expectations are met." She noted that the means of instilling a strong corporate culture will vary from company to company.

SEC Commissioner Aguilar on Cybersecurity. On June 10, 2014, in a speech titled *Boards of Directors, Corporate Governance and Cyber-Risks: Sharpening the Focus*, Commissioner Luis Aguilar discussed the board's role in addressing cybersecurity issues. Citing increases in the frequency and costs of cyber attacks, he stated that "ensuring the adequacy of a company's cybersecurity measures needs to be a critical part of a board of director's risk oversight responsibilities." As a starting point for assessing a company's possible cybersecurity measures, he suggested that boards consider using the Framework for Improving Critical Infrastructure Cybersecurity, released by the National Institute of Standards and Technology ("NIST") as a conceptual roadmap to begin assessing risks. In addition, he suggested that board's consider structural changes to assist in assessing cyber risk, including: mandatory cyber-risk education for directors; at least adequate representation on the board with a good understanding of information technology issues that pose risks to the company; and designating a separate enterprise risk committee of the board. He also encouraged boards to "put time and resources into making sure that management has developed a well-constructed and deliberate response plan" to address potential cyber event.

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