

# THE BOARD'S ROLE IN INTERMEDIARY OVERSIGHT

In January 2016, the SEC issued guidance on mutual fund distribution and sub-accounting fees intended to address considerations that have emerged with the changing distribution landscape and the rise in popularity of omnibus reporting with financial intermediaries. Consistent with its 1998 letter in which the SEC provided a framework for boards to consider in relation to fund supermarket fees and Rule 12b-1 compliance, the SEC reminds mutual fund boards of their duties to oversee the “reasonableness of fees.” The guidance goes on to suggest some specific considerations boards should consider when assessing intermediary relationships.

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## **SEC TO FUNDS' BOARDS: UNDERSTAND RELATIONSHIPS WITH INTERMEDIARIES**

Under the SEC's guidance, a mutual fund's board members need to be sure they understand:

- The core components of the fund's oversight program, which may include:
  - Fee negotiations and decisions
  - Fee invoicing and reconciliation
  - Operational oversight;
- The fund's intermediaries;
- The scope of services the intermediaries provide;
- The processes for negotiating and determining fees; and
- The fund's processes for evaluating quality of services (where it is possible to do so).

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The board of directors can rely on the fund's chief compliance officer to help make judgments about whether sub-accounting and other mutual fund paid fees represent payments for distribution. The fund's advisors and service providers should be able to provide relevant, organized information to help the board evaluate and oversee any intermediary arrangements.

### KNOW WHEN TO DIG DEEPER

What are some arrangements that may warrant closer attention?

- Tiered payment structures;
- Significant differences between fees or rates paid to similar intermediaries;
- Ensuring that other fees which are charged to the funds are not raised to cover distribution costs as an expense paid by another entity; and
- Distribution expenses and how they are paid in the absence of an active Rule 12b-1 plan.

### MEETING TODAY'S NEEDS AND PREPARING FOR THE FUTURE

While the SEC's focus on distribution in guise arose out of the complicated fee structures brought about by the trend toward omnibus recordkeeping, the evolution of the distribution landscape will continue. Likewise, the SEC's focus on fees and expenses is here to stay. When putting into place processes to oversee and clarify complex fee structures, keep in mind the ultimate goal of protecting and providing transparency to your end investors. Expect the program to evolve with the distribution landscape. A forward-thinking approach to assessing changes in distribution and service models, and how those changes will impact your fee arrangements and your intermediary relationships, will help you to adapt your programs for the future.

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Q59047 (6/16)