NORTHERN TRUST

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REGULATORY ADMINISTRATION DIGEST

Summarizing Developments in Investment Management Regulation

In this Issue

Any investment adviser filing an initial Form ADV or an amendment to an existing Form ADV on or after October 1, 2017 will be required to comply with the amendments to Form ADV.

SEC ADOPTS RULES TO ENHANCE INFORMATION REPORTED BY INVESTMENT ADVISERS

On August 25, 2016, the Securities and Exchange Commission (SEC) adopted amendments to the investment adviser registration and reporting form (Form ADV) to enhance the quality of information being reported and disclosed by investment advisers. The amendments to Form ADV are designed to provide additional information regarding investment advisers, including information about their (1) separately managed account business, (2) incorporate a method for private fund adviser entities operating a single advisory business to register using a single Form ADV, and (3) make clarifying, technical and other amendments to certain Form ADV items and instructions.

The amendments to Form ADV include several new disclosure requirements regarding separately managed accounts (SMAs). These amendments require investment advisers of SMAs to report (1) the types of assets; (2) the use of derivatives and borrowing; and (3) the role of custodians. The amount of information required to be reported is based on an investment adviser's total regulatory assets under management (RAUM) attributable to SMAs.

In addition, the amendments to Form ADV will require new disclosure information regarding an investment adviser's (1) identifying information; (2) advisory business; and (3) financial industry affiliations and private funds. More specifically, the new disclosures will include the following information:

- All investment adviser websites and all publicly available social media platforms;
- The total number of offices at which the investment adviser conducts investment advisory business and additional info rmation about their 25 largest offices;
- Confirmation of whether the investment adviser's chief compliance officer is compensated or employed by any person other than the investment adviser; and
- Investment adviser's balance sheet assets.

The amendments went into effect October 31, 2016. Any investment adviser filing an initial Form ADV or an amendment to an existing Form ADV on or after October 1, 2017 will be required to comply with the amendments to Form ADV. As SEC Chair Mary

Jo White explains, "These amendments are an important step in a series of rulemakings to enhance the SEC's monitoring and regulation of the asset management industry. Requiring investment advisers to report this additional information will provide investors and the Commission with a better understanding of the risk profile of each adviser and the industry as a whole."

KRISTIN SNYDER NAMED CO-HEAD OF SEC'S INVESTMENT ADVISER/ INVESTMENT COMPANY EXAMINATION PROGRAM

On August 10, 2016, the Securities and Exchange Commission (SEC) announced the appointment of Kristin Snyder as co-national associate director of the Investment Adviser/ Investment Company examination program in the Office of Compliance Inspections and Examinations (OCIE). OCIE is responsible for the SEC's National Examination Program, which examines SEC-registered investment advisers, investment companies, broker-dealers, self-regulatory organizations, clearing agencies and transfer agents. In addition to this role, Snyder will continue to serve as associate regional director for examinations at the SEC's San Francisco office, which she has held since November 2011.

As OCIE Director Marc Wyatt said, "With Kristin's experience in examinations and enforcement, she is well-positioned to develop and lead national initiatives in our investment adviser and investment company program that support OCIE's mission to improve compliance, prevent fraud, monitor risk, and inform policy."

Prior to her appointment, Snyder worked at the San Francisco SEC Enforcement Office for eight years serving as Branch Chief and Senior Counsel. Before joining the SEC, Snyder practiced at the law firm of Sidley Austin LLP in San Francisco.

With her appointment, Snyder joins Co-National Associate Director Jane Jarcho, who has led OCIE's Investment Adviser/Investment Company examination program since August 2013, and was named OCIE's Deputy Director in February 2016. Jarcho and Snyder oversee more than 520 lawyers, accountants and examiners responsible for the inspections of SEC-registered investment advisers and investment companies.

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> **MARC WYATT**
> OCIE Director

SIVOLELLA V. AXA EQUITABLE LIFE INSURANCE COMPANY: COURT RULING BODES WELL FOR REGISTERED INVESTMENT COMPANIES

On August 25, 2016, the United States District Court for the District of New Jersey ruled in Sivolella v. AXA Equitable Life Insurance Company and found the plaintiffs failed to show that the defendants, AXA, breached their fiduciary duty by charging excessive advisory and administrative fees to 12 AXA-sponsored mutual funds.

In this case, the AXA-sponsored mutual funds used a "manager of managers" model in which AXA

In its opinion, the court rejected the plaintiffs' assertion that AXA delegated all management to sub-advisors and sub-administrators. It found AXA was responsible for a range of management services, including services that were not listed in the advisory and administrative agreements.

served as the investment advisor to the funds but engaged sub-advisors and sub-administrators for the day-to-day management of the funds. The plaintiffs argued that because AXA allegedly delegated all of its advisory and administrative responsibilities to sub-advisors and sub-administrations, yet charged investors advisory and administrative fees above and beyond what it paid to the sub-advisors and sub-administrators for their services, those fees were excessive under Section 36(b) of the Investment Company Act of 1940.

In its opinion, the court rejected the plaintiffs' assertion that AXA delegated all management to sub-advisors and sub-administrators. It found AXA was responsible for a range of management services, including services that were not listed in the advisory and administrative agreements. The court also noted that AXA bore significant risks as the fund sponsor and advisor, including litigation and reputational risks. The court found that the management responsibilities that the advisor retained, combined with the various risks it bore as a result of that role, justified the advisory fees it charged to investors. The court reiterated the high bar imposed on 36(b) plaintiffs, namely, that liability requires proof that the advisor charged a fee that is "so disproportionately large that it bears no realistic relationship to the services rendered and could not be the product of arms-length bargaining."

OCIE ANNOUNCES SHARE CLASS EXAMINATION INITIATIVE

On July 13, 2016, the Office of Compliance Inspections and Examinations (OCIE) issued a National Exam Program Risk Alert regarding its new 2016 Share Class Initiative. The OCIE is seeking to address the risk that registered investment advisers may be making certain conflicted investment recommendations to their clients. The OCIE's Share Class Initiative will focus on identifying conflicts of interest tied to investment advisers' compensation or financial incentives for recommending mutual fund and 529 plan share classes that have substantial loads or distribution fees.

OCIE staff will focus on certain registered investment advisers and their associated persons that may be receiving undisclosed compensation or other financial incentives; and will conduct risk-based examinations that will focus on an investment advisers' share class recommendations, with a specific emphasis on fiduciary duty and best execution, disclosures, and compliance policies and procedures.