Report

New in RegTech:

SEC Marketing Rule Risk Alert, Private Funds Rule Verdict, & UK General Election Impact.

by:

Greg Hotaling
June 10, 2023

Marketing Rule compliance: SEC's recent Risk Alert

In April the SEC's Division of Examinations released its Risk Alert "Initial Observations Regarding Advisers Act Marketing Rule Compliance" (suggesting with the term "initial" that more risk alerts are to come, which the industry would welcome).

Among the Risk Alert's useful insights, is how firms' advertisements handle net fees (page 6). The SEC reports that, instead of actual client fees, some firms have been "using lower fees in calculations for net of fees performance returns than were offered to the intended audience".

Take the time to review the Risk Alert, as well as your firm's performance return calculations:

(1) Are the fees representative of the current fee structure?

(2) Are the share classes in performance returns disclosed?

(3) Is all material information provided?

Meanwhile, activity around Marketing Rule exam findings has been prolific, which our own Kyrstin Ritsema, Executive Director of Confluence Compliance Solutions Strategies, will discuss in NSCP Currents (regarding "Trends in SEC Marketing Rule Examinations").

Keep in mind that to comply properly with the Marketing Rule, investment advisers' implementation of measures such as risk assessments and mock SEC exams should take into account the recent Risk Alert and any further SEC guidance.

– Greg Hotaling, Regulatory Content Manager at Confluence

"In sharing these staff observations, the Division encourages advisers to reflect upon their own practices, policies, and procedures and to implement any appropriate modifications to their training, supervisory, oversight, and compliance programs"

SEC, Risk Alert, "Initial Observations Regarding Advisers Act Marketing Rule Compliance" (17 April 2024)

Fifth Circuit vacates SEC's Private Fund Adviser Rule

In In a victory for private fund advisers, on June 5th the Fifth Circuit Court of Appeals vacated the SEC's Private Fund Adviser Rule in its entirety, concluding in its opinion that the SEC had exceeded its statutory authority.

While the decision is not a complete surprise (see our analyses in February and May), it abruptly puts to rest adviser concerns about the Rule's nearing compliance dates in September 2024 and March 2025. (Even in a scenario where the SEC appeals successfully, those compliance dates should anyway be delayed.)

Meanwhile investor groups who favored the Rule are disappointed, but will maintain their push for more transparency. The Institutional Limited Partners Association (ILPA), for example, will continue its efforts to encourage detailed quarterly reporting from advisers and funds.

For more insight on the decision's implications, including a possible SEC appeal, see Sidley's piece "U.S. Fish Circuit Court of Appeals Vacates Private Funds Rules: What's Next?".

- Greg Hotaling, Regulatory Content Manager at Confluence

"While the Dodd-Frank Act expanded the Commission's oversight in many respects, it did not do so to the extent the Commission argues here ..."

> *NAPFM et al. vs SEC, Fifth Circuit Court of Appeals (Judge Englehardt, writing for 3-judge panel)*

How a new Labour government would impact financial services in the UK

In our March edition we looked at how an incoming Trump administration could affect financial regulation in the US. We now turn to the UK, where Prime Minister Rishi Sunak has requested a snap election for 4 July 2024 (granted by the King under the revived royal prerogative).

The UK election

Sunak's Conservative Party has faced gaping deficits in polls, averaging about 20% behind Labour during his 19 months as PM, following the historically brief and disastrous tenure of his Tory predecessor Liz Truss. Hence Sunak's call for an immediate general election -- which otherwise could have waited until January 2025 upon expiry of Parliament's 5-year term -- has some observers scratching their heads.

Whatever its rationale, the July 4th election is generating predictions of a large Parliamentary majority for Labour, with Opposition leader Keir Starmer as the new occupant of 10 Downing and Shadow Chancellor Rachel Reeves moving into Number 11 as head of HM Treasury. If the polling bears out, putting Labour in power for the first time in 14 years, what would it mean for financial regulation?

Labour's position

Following Labour's heavy defeat in 2019 when led by socialist Jeremy Corbyn, the party no longer appears eager to embrace its roots, according to some. Indeed on May 28th Reeves proclaimed, at a Rolls Royce factory, "I want to lead the most pro-growth, the most pro-business Treasury that our country has ever seen." Statements like this have formed part of Labour's "charm offensive" on the City, much to the annoyance of Conservatives.

Regarding Brexit, which Starmer strongly opposed while serving as Labour's "Brexit spokesman" under Corbyn, Labour's current position is that it would not seek to revisit that divisive issue. (In any case the UK could not unilaterally decide to re-join the EU. It would essentially need to show up with its tail between its legs, with re-accession needing the approval of all 27 EU countries -- a feat further complicated by Brexit's burned bridges.)

As for regulatory reforms recently enacted or in development, such as the landmark Financial Services and Markets Act 2023, Labour's Plan for Financial Services published in January noted that it would leave the reforms in place and instead "take a forward-looking approach". The Plan details Labour's policy priorities (growth and competitiveness, consumer protection, sustainability, fintech) and new initiatives (such as a streamlined FCA Handbook, a regulatory sandbox to develop products for underserved communities, and incentives for bonds secured by green assets). But it largely supports the current, ongoing work of UK financial authorities like the FCA, the Bank of England and the PRA. And so on its face, Labour's Plan doesn't threaten the wide-ranging Edinborough reforms and Mansion House reforms for financial services, already set in motion under Conservative Chancellor Jeremy Hunt.

Of course for investment managers, the UK's existing regulatory landscape already gives them plenty to consider. From SDR (see our February edition) to UK EMIR (see our April edition) and much more, compliance and operations departments are busy adjusting their workflows, and should expect those plans to continue under a Labour government.

For anticipating what else may come next, additional persons to watch include Reeves as well as Tulip Siddiq, the current Shadow City Minister (i.e., Shadow Economic Secretary to the Treasury). Note also that Labour's manifesto is to be released within the month, and can be requested here.

The FCA's next moves

It will be interesting to see whether decision-makers at the FCA, which is an independent body like the PRA and the Bank of England, nevertheless feel they could take more liberties under a Labour government. For example, with respect to enforcement. Already with Conservatives in power, controversially the FCA has proposed to publicly name firms it is investigating in certain cases, even before the outcome of such investigations. In response to a letter of concern about the proposal, from a House of Lords committee, the FCA had to acknowledge, among other things, that two-thirds of its investigations result in no action taken. Following a comment period that ended in April, the FCA reportedly will spend a few months thinking over its plans. (Would Labour coming to power give the FCA political cover for sticking to the proposal?)

In addition to vexing Conservatives and the City, this "naming and shaming" row has also renewed concerns about protecting FCA independence. While the FCA reports to the Treasury, which appoints the FCA's board, the FCA is also "an independent public body funded entirely by the fees we charge". An example of where that delicate line sits was perhaps seen in 2022, when the Government tried to introduce a "call-in power". It would have allowed Treasury to create, change or revoke financial regulators' rules if deemed in the public interest. When a barrage of criticism followed, including from FCA Chief Executive Nikhil Rathi, that call-in power was quickly scrapped.

So more recently when, in what was described as a "rare regulatory intervention", Chancellor Hunt expressed to the Financial Times his concern over the FCA's name-and-shame proposal, in fact it felt somewhat familiar. What has even been described as a long-running war between Westminster and the FCA.

For financial firms, the takeaway seems to be that under a government run by Labour, which is currently making all the right noises for the City, regulators like the FCA will nevertheless remain active as they continue to exercise their independence. This is supported in recent statements made by FCA Chair Ashley Alder on May 22nd and by Chief Executive Rathi on June 5th, in which they describe the FCA's path forward across many areas including private finance, retail investments, sustainable disclosures and innovation.

Meanwhile, the FCA is staying very busy regarding the wide swathe of EU-derived laws, including AIFMD, MiFID/MiFIR, MMFR, PRIIPs, the Short Selling Regulation and more, being dealt with in a post-Brexit UK. A handy table of the FCA's updated plans, for each such regime, can be found here.

And of course, if you're eligible to vote in the UK's general election, don't forget to register by June 18th.

- Greg Hotaling, Regulatory Content Manager at Confluence

"Labour will direct the FCA to issue an open call to industry to identify rules which have been made redundant by the Consumer Duty . . . Labour respects the FCA's independence in determining the appropriate changes in line with the Consumer Duty"

Financing Growth -- Labour's Plan for Financial Services, January 2024)

About Confluence

Confluence provides regulatory and investor communications solutions powered by data and analytics that make it easier to create, share and operationalize mission-critical reporting essential to the investment management industry.

Contact us here and explore our solutions here. Don't miss out on future monthly editions; subscribe to our newsletter!

Contact Us

confluence.com
info@confluence.com
+1 412 802 8632
@Confluence_News
@confluence-technologies