

Client Alert

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SEC Proposes Heightened Data and Reporting Rules for Funds and Advisers, Ponders New Rules on Derivatives and Leverage

By Jay G. Baris

At an open meeting of the Securities and Exchange Commission today, [Chair Mary Jo White](#) announced to enhance SEC reporting by [investment companies](#) and [investment advisers](#).

Data collection. The SEC proposed rules that would:

- Require funds and ETFs to provide additional data related to investments in derivatives, securities lending activities, liquidity and pricing of portfolio investments. These requirements would be designed to help the SEC assess potential risks to investors.
- Require funds to disclose certain basic risk metrics to help the SEC and investors better understand exposure to potential changes in risk factors and asset prices.
- Require investment advisers to file new categories of information with respect to separately managed accounts and the derivatives they hold.
- Modernize how data is transmitted to shareholders by requiring funds to provide investors with shareholder reports and portfolio information on fund websites, while preserving the ability of investors to request hard copies.
- Subject fund financial statements to enhanced and standardized disclosure requirements for derivatives and securities lending.

The Rules would require monthly reporting on Form N-PORT, which would require registered funds (other than money market funds) to report portfolio-wide and position-wide holdings data. The form would require monthly reports of investments, including:

- Data related to the pricing of portfolio securities;
- Information regarding repurchase agreements, securities lending activities and counterparty exposures;
- Terms of derivatives contracts; and
- Discrete portfolio level and position level risk measures to better understand fund exposure to changes in market conditions.

Client Alert

“Access equals delivery.” The proposal would permit registered funds, after satisfying certain conditions, to transmit shareholder reports by making them accessible on a website. Currently, funds must satisfy delivery requirements by printing and mailing shareholder reports, unless investors affirmatively request the fund to deliver the reports electronically.

While the “access equals delivery” model would result in cost savings, Commissioner Luis Aguilar noted that “it could also result in unintended consequences, such as creating unnecessary hurdles that could discourage shareholders from reading the shareholder reports.”

The rules would allow investors to ask for paper copies, and funds must inform investors using plain English how to obtain paper copies.

Investment adviser registration. The SEC proposes to amend Form ADV to require additional information for the SEC and investors to better understand the risk profile of individual advisers and the industry as a whole. Among other things, the rules would:

- Require aggregate information related to assets held and use of borrowings and derivatives in separately managed accounts.
- Permit by rule certain “umbrella registration” filing arrangements that are currently outlined in staff guidance.
- Provide additional information about an adviser’s advisory business, including branch office operations and the use of social media.

Investment Advisers Act rules. Proposed amendments to the rules under the Investment Advisers Act would require advisers to maintain records of the calculation of performance information that is distributed to any person. Currently, advisers must maintain performance information that is distributed to ten or more persons. The proposed amendments also would require advisers to maintain communications related to performance or rate of return of accounts and securities recommendations.

Oversight of investment advisers. Chair White said that the staff is also forming recommendations to enhance the management and disclosure of liquidity risk by mutual funds and ETFs and to “update liquidity standards” for mutual funds and ETFs. The staff is considering, among other things, proposals for:

- Specific requirements for the use of derivatives by funds, including limits on leverage and enhanced risk management programs for derivatives and leverage;
- Stress testing by large investment advisers and large funds; and
- Transition planning for addressing major disruptions in an investment adviser’s operations.

Our take. The SEC’s efforts to require enhanced reporting, enhanced risk management and transition planning should come as no surprise following statements from federal banking regulators and the Financial Stability Oversight Council (FSOC) that asset managers present systemic risks to the U.S. financial markets. We believe that the SEC, not the federal banking regulators, is best positioned to address these risks, and the SEC must take control of this debate.

Client Alert

The SEC seems poised to make specific recommendations concerning investment company use of derivatives and leverage. Any specific proposals come nearly four years after the SEC published a [concept release](#) requesting public comment on this topic. The devil is in the details, of course, and any attempt to limit use of derivatives is sure to generate much public debate, so we don't expect any significant changes to come any time soon.

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