2019 and Q1 2020 Developments and Annual Compliance Checklists

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Lowenstein Sandler's Investment Management Group is pleased to provide you with (i) a summary of recent legislative and regulatory developments that impact the investment management community; and (ii) checklists of annual considerations for private investment funds, investment advisers, commodity trading advisors, and commodity pool operators. The checklists appear after the legislative and regulatory summary. For more information regarding any matter covered in this update, please contact one of the attorneys in our Investment Management Group.

SELECT LEGISLATIVE AND REGULATORY DEVELOPMENTS

Financial Industry Regulatory Authority, Inc. ("FINRA") Amendments to Rules 5130 and 5131

Synopsis: On November 5, 2019, the Securities and Exchange Commission (the "SEC") approved FINRA's amendments to Rules 5130 and 5131 to help facilitate capital raising and to ease the administrative burden of the new issue distribution restriction.

Status: FINRA Rules 5130 and 5131, which work in tandem, help ensure the initial public offering process is fair by restricting certain securities from being distributed to restricted persons who possess an insider status or who could inure a quid pro quo benefit by participating in the distribution (commonly referred to as "spinning").

FINRA Rules 5130 and 5131 have been updated to broaden exemptions allowing for the allocation of new issues in relation to certain sovereign wealth funds, foreign investment companies, employee benefit plans, family offices, and officers and directors of charities. FINRA Rules 5130 and 5131 have been harmonized to provide regulatory consistency with respect to issuer-directed allocations and anti-dilution exemptions and updated to expressly exclude foreign offerings (not available if the foreign offering is made concurrently with a domestic offering) and offerings of special purpose acquisition company interests.

Private fund managers should:

- Update their subscription agreements to reflect the new exceptions to FINRA Rules 5130 and 5131.
- Update their annual investor certifications to reflect the new exceptions to FINRA Rules 5130 and 5131.
- Given the broadened exemptions, reassess whether each of their private funds may now be unrestricted by qualifying for the de minimis exemption for entities in which a limited percentage of new issues profits and losses are held by, or shared with, restricted persons.
- Recalculate the allocation of new issues participation, and the expenses associated with that participation, within their private funds on a go-forward basis.

Other investment managers should update their investment policy statements and investment management agreements to reflect the new exceptions to FINRA Rules 5130 and 5131.

For additional information regarding amendments to FINRA Rules 5130 and 5131, please see the below links:

- FINRA Proposing Release
- FINRA Amendment
- SEC Approval Order
- FINRA Reg. Notice 19-37

The Lowenstein Sandler LLP Investment Management Group alert analyzing FINRA'S amendments to FINRA Rules 5130 and 5131 is available here.

Regulation Best Interest and Form Client Relationship

Synopsis: On June 5, 2019, the SEC adopted Regulation Best Interest ("Reg. BI"), which alters the standard of conduct a broker-dealer, including dual registrants acting in the capacity of a broker-dealer, and its associated persons must maintain when making recommendations to retail investors. FINRA has published a Reg. BI and Form Client Relationship Summary ("Form CRS") Firm Checklist providing guidance, including best practices, for broker-dealers and investment advisers, including those that are dual registrants, to comply with Reg. BI and Form CRS. Reg. BI has a June 30, 2020 compliance date.

Status: Broker-dealers must abide by a suitability standard codified in FINRA Rule 2111. This standard requires broker-dealers to have a reasonable basis, after conducting reasonable diligence, for believing that their recommendation is suitable for their customers. Reg. BI builds on this standard, requiring broker-dealers to act in the "best interest" of their customers when making a recommendation. To effectuate this goal, Reg. BI creates four interrelated obligations, as defined by Reg. BI: (i) disclosure; (ii) care; (iii) conflict of interest; and (iv) compliance. The conflict of interest and compliance obligations apply solely to the broker-dealer, whereas disclosure and care obligations apply jointly to the broker-dealer and its associated persons.

Reg. BI applies to broker-dealers interacting with retail investors whenever they are recommending any account type, security, or investment strategy. This differs from the current standard by explicitly including account type recommendations (e.g., IRAs, brokerage, advisory). A broker-dealer must take into account factors such as cost, alternatives, and the customer investment profile in making this recommendation. While what constitutes a recommendation remains consistent with current FINRA guidance, new express elements of consideration have been added, including care, skill, and cost. A broker-dealer must now always consider cost, both at the time of the recommendation and at potential liquidation.

In the recently released checklist, FINRA clarified expectations related to the implementation of Reg. BI. However, FINRA has been silent regarding how Reg. BI will interplay with its existing rules, including FINRA Rule 2111.

The SEC also recently adopted Form CRS, which will require investment advisers, broker-dealers, and dual registrants to provide retail investors with a brief summary regarding their relationship. Unlike Reg. BI, which applies only to broker-dealers and dual registrants, Form CRS applies to investment advisers, broker-dealers, and dual registrants with retail customers, irrespective of whether they provide recommendations. The relationship summary is intended to inform retail investors about the types of client and customer relationships and services the investment adviser and/or broker-dealer offers, as well as the fees, costs, conflicts of interest, and applicable standards of conduct associated with those relationships and services.

For additional information regarding Reg. BI, Form CRS, and the FINRA checklist, you can reference the following resources:

- FINRA Reg. BI Website
- SEC Reg. BI: A Small Entity Compliance Guide
- SEC Form CRS: A Small Entity Compliance Guide
- SEC Form CRS: Instructions

The Lowenstein Sandler LLP Investment Management Group alerts analyzing Reg. BI and Form CRS are available here, here, and here.

Proposed Updates to Advertising and Solicitation Rules

Synopsis: On November 4, 2019, the SEC published in a more than 500-page proposing release an update to its advertising and solicitation rules for investment advisers, to modernize the rules governing how an investment adviser may attract clients and private fund investors. The proposal seeks primarily to update Section 206(4)-1 and Section 206(4)-3 of the Investment Advisers Act of 1940 (as amended, the "Advisers Act") to a more principles-based construct that is responsive to technological developments and the diverse types of investment advisers now under the SEC's purview.

Status: The proposal's amendments to the advertising rule, found primarily in Section 206(4)-1 of the Advisers Act, aim to create a more tailored and principles-based regime. The proposal seeks to reflect market developments since the advertising rule's adoption in 1961, including changes in: (i) technology used for communications; (ii) expectations of investors shopping for advisory services (e.g., ability to seek out reviews and information to evaluate products and services); and (iii) the nature of the investment advisory industry (e.g., types of investors seeking and receiving services). Specifically, the SEC is proposing to: (i) modify the definition of "advertisement" to be more "evergreen" in light of today's ever-changing technology; (ii) replace the four per se prohibitions with principles that are reasonably designed to prevent fraudulent or misleading conduct and practices; (iii) allow for the use of testimonials, endorsements, and third-party ratings with restrictions and conditions; and (iv) include tailored requirements for the presentation of performance results, based on an advertisement's intended audience.

The solicitation rule found in Rule 206(4)-3 of the Adviser Act provides, among other things, disclosure of potential bias a solicitor may have when attempting to attract clients or private fund investors for an investment adviser (the "solicitation disclosure"). Since its adoption, the advisory industry has evolved and grown, while the solicitation rule has remained static. The proposal's solicitation changes focus on updating: (i) the solicitation disclosure's scope (including application of Rule 206(4)-3 to private fund investors as well as advisory clients), format, substance, and compliance; (ii) the types of ineligible solicitors; and (iii) exemptions from the solicitation disclosure.

The Lowenstein Sandler LLP Investment Management Group alert analyzing the SEC's proposed updates to its advertising and solicitation rules is available here.

SEC Issues Proxy Voting Guidance

Synopsis: On August 21, 2019, the SEC issued additional guidance to investment advisers pertaining to proxy voting, including the fiduciary duty under Rule 206(4)-6 of the Advisers Act, and required disclosures under the Investment Company Act of 1940 (as amended, the "Investment Company Act"). In question-and-answer format, the SEC set forth best practices for investment advisers engaged in proxy voting, including establishing and exercising the scope of the investment adviser's authority and responsibilities, demonstrating that voting determinations are in a client's best interest, and additional considerations when retaining proxy advisory firms to assist with discharging proxy voting duties. As a result of litigation challenging the SEC's guidance, the SEC has agreed that it will not invoke the guidance as an independent source of binding law in any enforcement or regulatory action until the earlier of January 1, 2021, or the issuance of final rules in the SEC's proxy advisor rulemaking. However, the guidance remains a reflection of the SEC's interpretation of underlying statutes and regulations.

Status: As detailed in the SEC's guidance, all investment advisers owe fiduciary duties to their clients under the Advisers Act. An investment adviser's fiduciary duty as it relates to proxy voting will vary with the scope of the voting authority assumed by the investment adviser. An investment adviser and its client may shape the scope of the advisory relationship, including voting authority, through full and fair disclosure by the investment adviser and informed consent by the client. Under all circumstances, an investment adviser that assumes proxy voting authority for a client must make voting determinations consistent with its fiduciary duty and in compliance with Rule 206(4)-6 of the Advisers Act, which requires said investment adviser to adopt and implement policies and procedures that are reasonably designed to ensure execution of its voting authority is in its clients' best interest.

An investment adviser with voting authority may satisfy its duty of care by gaining a reasonable understanding of its client's objectives and making voting determinations that are in its client's best interest. Investment advisers also have an obligation under Rule 206(4)-6 of the Advisers Act to "adopt and implement written policies and procedures that are reasonably designed to ensure that the investment adviser votes proxies in the best interest of its clients." The SEC suggests that an investment adviser consider the following factors when evaluating whether voting determinations are in a client's best interest and in accordance with the investment adviser's proxy voting policies and procedures: (i) whether it is in a client's best interest to adopt and implement uniform or bespoke proxy voting policies and procedures, taking into account the client's investment strategy and objectives; (ii) whether to conduct a more detailed analysis of a specific issue or matter to ensure that voting determinations are not based on materially inaccurate or incomplete information; and (iii) whether to sample proxy votes and/or adopt additional measures, as necessary, to determine compliance with policies and procedures and ensure that votes were cast in a client's best interest.

An investment adviser should conduct appropriate diligence when retaining a proxy advisory firm for research or voting recommendations. The measures an investment adviser takes to determine whether to retain a proxy advisory firm may vary based on the scope of the investment adviser's voting authority and the services the proxy advisory firm is engaged to perform. Investments advisers should adopt and implement comprehensive policies and procedures to review and assess proxy advisory firms and their services. Investment advisers should also consider requiring proxy advisory firms to provide regular, ongoing updates regarding relevant business changes. If an investment adviser is made aware of potential factual errors, methodological weaknesses, or other defects or inadequacies in a proxy advisory firm's analysis that may materially affect the investment adviser's voting determination, then it should conduct a reasonable investigation into the matter.

One of the two largest proxy advisory firms, Institutional Shareholder Services, has filed a lawsuit against the SEC challenging the SEC's guidance. As part of a stay of the lawsuit, the SEC has agreed that it will not invoke the guidance as an independent source of binding law in any enforcement or regulatory action until the earlier of January 1, 2021, or the issuance of final rules in the SEC's proxy advisor rulemaking.

The SEC's guidance is available here. The Lowenstein Sandler LLP Investment Management Group alert analyzing the SEC's proxy voting guidance is available here.

SEC Interpretation on Fiduciary Duties of Investment Advisers

Synopsis: On June 5, 2019, the SEC issued an interpretation to clarify its position on fiduciary duties of investment advisers. The interpretation emphasized how client sophistication and the scope of an advisory relationship affect the fiduciary duties owed to particular clients.

Status: The interpretation discussed the importance of determining the nature and scope of the client relationship in order to determine the extent of the fiduciary duties. The SEC detailed more obligations for advisers serving retail investors than for advisers serving institutions, including private funds. The interpretation discusses the duty of care (including the duty to provide advice in the best interest of the client, the duty to seek best execution, and the duty to provide advice and monitoring over the course of the client relationship) and the duty of loyalty (including the duty to subordinate the adviser's interests to its clients' interests, the duty to disclose material facts and conflicts of interest, and duties in relation to allocating investment opportunities).

Advisers of private funds must largely adhere to their advisory agreements and other organizational and offering documents containing specific disclosure in order to uphold their duty of care and duty of loyalty. In contrast, advisers serving retail investors must periodically update their understanding of an individual's changing investment goals and offer more details in disclosing conflicts (which must be relatively simple to understand).

Advisers of retail investors in particular should revisit their operations to ensure that they are keeping up with clients' goals and tailoring disclosures based on clients' levels of sophistication. Advisers of private funds should review their governing documents and disclosure practices to make sure they reflect the services provided.

The SEC's interpretation on fiduciary duties of investment advisers is available here. The Lowenstein Sandler LLP Investment Management Group alert analyzing the SEC's interpretation is available here.

SEC's Office of Compliance Inspections and Examinations ("OCIE") Releases 2020 Examination Priorities for Investment Advisers, Broker-Dealers, and Other Financial Industry Professionals

Synopsis: On January 7, 2020, OCIE published its 2020 Examination Priorities (the "2020 Exam Priorities") for its National Exam Program. The 2020 Exam Priorities share many of the same concerns OCIE expressed in its 2019 Examination Priorities. Both focus on the protection of retail clients/investors, including the standard of care given to clients/investors and the marketing of popular retail client/investor investments (e.g., mutual funds and exchange-traded funds), the need for robust information security and cybersecurity policies, the regulation of digital assets (e.g., Bitcoin), review of anti-money laundering ("AML") programs, the protection of critical market infrastructure, and OCIE's oversight of FINRA and the Municipal Securities Rulemaking Board ("MSRB").

Status: OCIE emphasized the following in the 2020 Exam Priorities:

Protection of Retail Investors. The protection of retail clients/investors, especially those who, historically, have been victimized by unscrupulous advisers and brokers (e.g., seniors, teachers, and military personnel), is paramount to OCIE. Firms with retail clients/investors or firms that market products to retail clients/investors (e.g., mutual funds, exchange-traded funds, and municipal securities) should prepare for exams focused on disclosure of fees, expenses, compensation arrangements, and conflicts of interest, as well as supervision of outside business activities of employees and associated persons.

Holistic Information Security Policies and Procedures. Due to the heightened risk of cybersecurity attacks, the SEC views robust information security programs as critical to protecting client/investor information, market security, and integrity. For that reason, OCIE's 2020 exams will focus on: (i) proper configuration and monitoring of network storage devices; (ii) governance and risk management policies; (iii) access control policies, especially for firms that offer access online and/or via a mobile application; (iv) data loss prevention policies and procedures; (v) vendor and network management and oversight, especially for firms that utilize cloud-based storage; (vi) training of staff on cybersecurity concerns; (vii) incident response and resiliency; and (viii) appropriate disposal of retired hardware that may contain client/investor information and/or potential network information.

Review of Firms That Leverage Fintech and Innovative Technologies. Firms that utilize "alternative data" and other innovative technology to drive investment decisions or trading automation should be prepared to show how the firm uses data and technology to interact with and provide services to clients/investors and service providers. OCIE notes that digital assets present particular risks for retail clients/investors who do not appreciate the differences between digital assets (such as Bitcoin) and more traditional products. Due to what the SEC perceives as a general lack of awareness and understanding of digital assets, OCIE will prioritize exams of firms that provide services related to digital assets. Similar to what we have seen from OCIE over the past three years, robo- or digital advisors can anticipate OCIE seeking information in the form of a limited or more extensive examination relatively soon after effectiveness of registration.

Review of AML Programs. Broker-dealers and investment companies should ensure that they have adequate policies and procedures in place that are reasonably designed, based on such firms' business, to identify suspicious activity and illegal money-laundering activities.

The Protection of Market Infrastructure. OCIE continues to recognize the importance of the security and resiliency of services critical to the functioning of U.S. capital markets (e.g., clearing agencies, national securities exchanges, alternative trading systems, and transfer agents). OCIE will continue to conduct exams of these service providers in an effort to assess the risks they face and the ability of such service providers to respond to these risks in a timely and effective manner.

FINRA and MSRB. OCIE's oversight investigations and examinations of FINRA and MSRB will continue to focus on the protection of clients/investors and market integrity. In its investigations, OCIE will collect and analyze extensive information and data, conduct meetings with key personnel, and reach out to various stakeholders, including broker-dealers and investor groups. OCIE will then make detailed recommendations to improve FINRA's and MSRB's programs and policies, risk assessment processes, and future examinations.

Additional Market Participant-Specific Focus Areas. OCIE also highlighted the following focus areas for certain market participants based on services provided: (i) for broker-dealers, exams will focus on compliance with the Customer Protection and Net Capital Rules as well as broker-dealers' trading and risk management practices; (ii) for registered investment advisers, exams will focus on Rule 206(4)-7 compliance programs and new or emerging investment strategies; and (iii) for municipal advisors, OCIE is also prioritizing the review of a municipal advisor's fiduciary duty obligations, fair dealing with market participant requirements, disclosure of conflicts of interest, and compliance with MSRB Rule G-40 concerning advertisements.

The full text of OCIE's risk alert can be found here. The Lowenstein Sandler LLP Investment Management Group alert analyzing OCIE's risk alert is available here.

Financial Industry Regulatory Authority ("FINRA") Risk Monitoring and Examination Priorities for 2020

Synopsis: On January 9, 2020, FINRA announced its 2020 Risk Monitoring and Examination Priorities Letter (the "2020 Priorities Letter"). The 2020 Priorities Letter shares several focus areas with FINRA's 2019 Risk Monitoring and Examination Priorities Letter. Among other items, both address FINRA's concern regarding sales practices and suitability, emerging digital asset business models, and cybersecurity policies and procedures.

FINRA is also implementing an integrated examination program, categorizing firms by the following business models: retail, capital markets, carrying and clearing, trading and execution, and diversified. This new examination structure allows FINRA to better align risk profiles with broker-dealers.

Status: FINRA's 2020 risk monitoring and examination priorities reflect guidance for FINRA-regulated members regarding areas that it will pay most attention to this year, falling under several broader categories: (i) sales practice and supervision, including in relation to Reg. BI and Form CRS, communications with the public, and cash management and bank sweep programs; (ii) market integrity, including in relation to best execution and the vendor display rule; (iii) financial management, including in relation to the Customer Protection and Net Capital Rules, digital assets, and liquidity management; and (iv) firm operations, including in relation to customer confirmations, anti-money laundering compliance, cybersecurity, and technology governance.

For additional information regarding FINRA's 2020 Priorities Letter, please see FINRA 2020 Letter, FINRA President Cover Letter, and FINRA Risk Monitoring Structure Announcement. The Lowenstein Sandler LLP Investment Management Group alert analyzing FINRA'S risk monitoring and examination priorities is available here.

SEC's Division of Enforcement Annual Report

Synopsis: On November 6, 2019, the SEC's Division of Enforcement (the "Division") published its fiscal year 2019 Annual Report, which details the Division's fiscal year 2019 accomplishments and key initiatives.

Status: Overall, enforcement actions, disgorgement and penalties, and monies returned to harmed investors increased as compared to fiscal year 2018. The 2019 Annual Report articulated the Division's five core principles: (i) focus on the retail investor; (ii) focus on individual accountability; (iii) keep pace with technological change; (iv) impose remedies that most effectively further enforcement goals; and (v) constantly assess the allocation of resources.

The Lowenstein Sandler LLP alert analyzing the Division's 2019 Annual Report is available here.

Common Compliance Failures With Regard to Principal Trades and Agency Cross Trades

Synopsis: OCIE recently issued an alert listing the most common compliance failures that investment advisers commit with regard to principal trades and agency cross trades. Specifically, OCIE observed that advisers often overlook the notice and consent requirements associated with these trades. This oversight tends to occur when advisers' policies are insufficient or are not followed in fast-paced trading practices.

Status: A "principal trade" occurs when an investment adviser, acting as a principal for its own account, knowingly (i) sells any security to a client; or (ii) purchases any security from a client. Section 206(3) prohibits advisers from making principal trades unless the adviser discloses all material information about the proposed trade to, and obtains the consent of, such client *before* the completion of the transaction. Notably, blanket disclosure and consent do not suffice, disclosure and consent are required for each such transaction.

An "agency cross transaction" occurs when an investment adviser, acting as broker for a person other than the advisory client, knowingly makes a sale or purchase of any security for the account of that client. Section 206(3) prohibits investment advisers from making agency cross trades unless the investment adviser discloses material information about the trade to the client before the completion of the sale or purchase and obtains the consent of the client to such transaction. Notably, if the investment adviser takes additional precautions under Rule 206(3)-2, it *may* not be required to effect transaction-by-transaction disclosure and consent for certain agency cross transactions. Section 206(3) should be read together with Sections 206(1) and (2) so that the adviser further discloses any potential conflicts of interest invoked by a trade.

OCIE highlighted the following examples of common investment adviser compliance deficiencies with respect to principal trades and agency cross trades:

Failure to Recognize Nature of Trade. Firms may fail to recognize that a trade was a principal trade subject to Section 206(3) and thus to make the required disclosures and obtain the required consents (or if the principal trade was recognized as such, do not making adequate disclosure/obtain adequate consent (e.g., obtaining consent after the completion of the trade)).

Nonadherence to Policies and Procedures. Firms may fail to produce documentation evidencing compliance with internal compliance policies and procedures and applicable law or fail to establish Section 206(3) policies and procedures. Further, if such policies were established, firms may fail to follow such policies and procedures.

The Lowenstein Sandler LLP Investment Management Group alert analyzing OCIE's risk alert is available here.

National Futures Association's Swaps Proficiency Requirements and Amendments to Compliance Rule 2-34

Synopsis: In a March 5, 2019, submission letter to the Commodity Futures Trading Commission ("CFTC"), the National Futures Association ("NFA") indicated that any individual applying for approval as a Futures Commission Merchant ("FCM"), Introducing Broker ("IB"), Commodity Pool Operator ("CPO") or Commodity Trading Advisor ("CTA") Member swap firm or swap associated person of an FCM, IB, CPO, or CTA Member shall not be granted approval as a swap firm or swap associated person unless they have taken and passed the NFA's swaps proficiency examination. On September 12, 2019, the NFA released updated Frequently Asked Questions ("FAQ") regarding the new swaps proficiency requirements.

In an August 29, 2019, submission letter to the CFTC, the NFA amended NFA Compliance Rule 2-34 in relation to performance reporting and disclosures.

Status: The NFA requires that associated persons engaging in commodity futures and forex activities take and pass a proficiency examination that tests both their market knowledge and their knowledge of regulatory requirements. The NFA determined that associated persons engaging in swaps activities at FCMs, IBs, CPOs, and CTAs, as well as individuals acting as associated persons at swap dealers ("SDs") and Major Swap Participants ("MSPs"), should be required to meet a minimum proficiency standard that tests both their market knowledge and their knowledge of regulatory requirements involving swaps activities. Accordingly, NFA has imposed proficiency requirements on individuals approved as swap associated persons at FCMs, IBs, CPOs, and CTAs. NFA is also requiring that SD and MSP Members ensure that individuals acting as associated persons have satisfied the swaps proficiency requirements. Individuals have until January 31, 2021, to complete these requirements.

NFA Compliance Rule 2-34 now requires written confirmation for accounts with actual funds that differ from nominal account size. If any changes are made to the client's trading program or nominal account size or the way in which cash additions, cash withdrawals, or net performance affect nominal account size, a written confirmation describing these changes must be provided to or received from the client prior to the CTA placing any new trades for the client. In the absence of a written confirmation designating a nominal account size, performance returns must be based on the amount of actual funds.

The NFA's submission letter detailing the swaps proficiency requirements is available here. The NFA's FAQ regarding the swaps proficiency requirements is available here.

National Futures Association's Amendments to Compliance Rules

Synopsis: Through August 29, 2019, submission letters to the CFTC, the NFA: (i) amended an interpretive notice in relation to NFA Compliance Rule 2-13 concerning break-even analyses; (ii) amended an interpretive notice in relation to NFA Compliance Rule 2-34 concerning performance reporting and disclosures; and (iii) amended NFA Compliance Rules 2-29 and 2-36 (and several related interpretive notices) concerning communications with the public and use of promotional materials.

Status: Amendments to the interpretive notice for NFA Compliance Rule 2-13 disallow certain interest income in the break-even analysis where not expected to offset expenses. NFA Compliance Rule 2-34 now requires written confirmation for accounts with actual funds that differ from nominal account size. If any changes are made to the client's trading program or nominal account size or the way in which cash additions, cash withdrawals, or net performance affect nominal account size, a written confirmation describing these changes must be provided to or received from the client prior to the CTA placing any new trades for the client. In the absence of a written confirmation designating a nominal account size, performance returns must be based on the amount of actual funds.

NFA Compliance Rule 2-29 was amended to: (i) limit to FCM, IB, CPO and CTA Members; (ii) expand the scope to all commodity interest (not just futures-related) activities; (iii) specify that certain forms of audio and video promotional materials making specific trade recommendations or discussing profits be submitted for NFA review and approval; and (iv) modifying the Regulation 4.7 exemption to request compliance with the hypothetical performance disclaimer requirements. NFA Compliance Rule 2-36 was amended to specify that forex dealer Members and their associates must comply with certain provisions of NFA Compliance Rule 2-29.

The NFA's submission letter detailing the amendments to NFA Compliance Rules 2-13 and 2-34 is available here. The NFA's submission letter detailing the amendments to NFA Compliance Rules 2-29 and 2-36 is available here.

CFTC Amendments to Part 4 Regulations

Synopsis: Effective January 9, 2020, the CFTC amended several rules applicable to CPOs and CTAs.

Status: The amendments include provisions: (i) codifying prior relief providing that certain family offices will be exempt from CPO and CTA registration; (ii) providing that investment advisers to business development companies and any registered investment company will generally be excluded from the definition of CPO; (iii) providing that general solicitation will be expressly permitted for certain exempt pools consistent with the Jumpstart Our Business Startups Act; (iv) providing that non-U.S. persons will be expressly permitted in pools subject to a 4.13(a)(3) de minimis exemption; and (v) providing that non-U.S. pools may maintain books and records in the location of the non-U.S. pool.

Further information on the CFTC's amendments discussed above is available here and here.

SEC Proposes to Update Accredited Investor and Qualified Institutional Buyer Definitions

Synopsis: On December 18, 2019, the SEC proposed amendments to the definitions of accredited investor and qualified institutional buyer. The amendments would allow more investors to participate in private offerings by adding new categories of persons that may qualify as accredited investors based on their professional knowledge, experience, or certifications. The proposal would also expand the list of entities that may qualify as accredited investors by, among other things, allowing any entity that meets an investments test to qualify.

Status: The proposed amendments to the accredited investor definition would add new categories of natural persons based on professional knowledge, experience, or certifications. The proposed amendments would also add new categories of entities, including a "catch-all" category for any entity owning in excess of $5 million in investments. In particular, the proposed amendments to the accredited investor definition would add: (i) a category based on certain professional certifications and designations, such as a Series 7, 65, or 82 license, or other credentials issued by an accredited educational institution; (ii) a new category based on the person's status as a "knowledgeable employee" with respect to a private fund; (iii) limited liability companies that meet certain conditions, registered investment advisers, and rural business investment companies ("RBICs") to the current list of entities; (iv) a new category for entities owning investments in excess of $5 million; (v) family offices with at least $5 million in assets under management (and their family clients); and (vi) spousal equivalents that may pool their finances for the purpose of qualifying as accredited investors.

The proposed amendments to the qualified institutional buyer definition in Rule 144A would add limited liability companies and RBICs to the types of entities that are eligible for qualified institutional buyer status if they meet the $100 million in securities threshold in the definition. The proposed amendments would also add a "catch-all" category that would permit institutional accredited investors under Rule 501(a), of an entity type not already included in the qualified institutional buyer definition, to qualify as qualified institutional buyers when they satisfy the $100 million threshold.

The SEC's proposed rule detailing the amendments is available here.

9th Circuit Rules in Favor of hiQ in Its Web Scraping Dispute With LinkedIn

Synopsis: The U.S. Court of Appeals for the 9th Circuit recently issued its long-awaited ruling in hiQ Labs, Inc. ("hiQ") v. LinkedIn Corporation ("LinkedIn"). The 9th Circuit ruled that LinkedIn cannot prevent hiQ from scraping the profiles of LinkedIn's members if those profiles are "available for viewing by anyone with a web browser."

Status: This case has been closely watched by investment advisers that scrape web data (and vendors that supply web-scraped data to investment managers), as the lower court's ruling was the first significant federal or state court ruling specifically addressing the validity of web scraping and whether information on a website is considered "public."

For investors who employ web-scraped data as part of their investment research process, guidance on whether website information is public or private is of critical importance. Under U.S. securities laws, an investor cannot be found guilty of insider trading if the government cannot prove that the information it possessed was nonpublic. Although the hiQ case is not directly concerned with insider trading, the 9th Circuit's decision provides investors with "first-of-its-kind" legal guidance on whether information on the internet (whether scraped or simply viewed with a browser) is public or nonpublic. The 9th Circuit concluded that information on a website is part of the public domain, and thus freely accessible by users and scrapers alike (i.e., publicly available information), so long as it (i) does not require a username, password, or other form of authentication in order to access it; or (ii) is not demarcated as private using such an authorization system.

A copy of the 9th Circuit's opinion is available here. The Lowenstein Sandler LLP Investment Management Group alert analyzing the 9th Circuit's decision is available here.

Preparedness for LIBOR Transition

Synopsis: The United Kingdom's Financial Conduct Authority announced in 2017 that it would no longer compel LIBOR panel banks to furnish data to support the determination of the reference rate known as the London Interbank Offered Rate ("LIBOR") after 2021. As a result, LIBOR is unlikely to continue past the end of 2021. Pursuant to a December 23, 2019, industry letter, the New York State Department of Financial Services has required that each regulated institution submit a response by February 7, 2020, describing the institution's plan to address its LIBOR cessation and transition risk.

Status: The Board of Governors of the Federal Reserve ("FRB"), and the Federal Reserve Bank of New York ("FRBNY"), in conjunction with the U.S. Treasury Department's Office of Financial Research, have created a new rate called the Secured Overnight Financing Rate ("SOFR"), which the FRBNY has been publishing since April 2018. SOFR measures the cost of overnight borrowings through repo transactions collateralized with U.S. treasuries. After evaluating a range of possible alternative rates, the Alternative Reference Rates Committee, convened by the FRB and the FRBNY, has chosen SOFR as its recommended alternative to U.S. dollar LIBOR and continues to work through transition issues and provides guidance on the process.

Response plans are required of all institutions regulated by the New York State Department of Financial Services: depository institutions (including banks, credit unions, and savings associations); nondepository institutions (including licensed lenders, sales finance companies and premium finance companies, mortgage companies, money transmitters, and virtual currency companies); property insurance companies; health insurance companies; and life insurance companies and pension funds. The plans should describe: (i) programs that would identify, measure, monitor, and manage all financial and nonfinancial risks of transition; (ii) processes for analyzing and assessing alternative rates, and the potential associated benefits and risks of such rates both for the institution and its customers and counterparties; (iii) processes for communications with customers and counterparties; (iv) a process and plan for operational readiness, including related accounting, tax, and reporting aspects of such transition; and (v) the governance framework, including oversight by the board of directors, or the equivalent governing authority, of the regulated institutions.

The New York State Department of Financial Services' industry letter is available here.

Qualified Opportunity Funds

Synopsis: The Tax Cuts and Jobs Act passed in December 2017 included a provision (Section 1400Z-2 of the Internal Revenue Code) that creates the ability to defer tax on certain capital gains and sometimes even avoid those taxes by investing in a qualified opportunity fund ("QOF"). If a taxpayer engages in a taxable sale or exchange with an unrelated person before 2027, the taxpayer may defer capital gain arising from that sale or exchange ("Deferred Gain") by making an equity investment in a QOF (in an amount equal to the desired amount of gain deferral) during the 180-day period beginning on the date the property is sold or exchanged, subject to certain exceptions and special rules for certain gains (e.g., where a pass-through recognizes taxable gain and Section 1231 gains). There are three key tax benefits of investing Deferred Gain in a QOF. First, Deferred Gain is included in the investor's income when the "investment" is sold or exchanged or, if earlier, December 31, 2026 (the "Gain Inclusion Date") (the Deferred Gain may be reduced to the extent the fair market value of the QOF interest decreases).

Accordingly, if the investor does not dispose of the QOF investment in a taxable transaction before December 31, 2026, the investor generally defers the recognition of the Deferred Gain until December 31, 2026. Second, if the investor has held the QOF investment for at least five years on the Gain Inclusion Date, 10 percent of the Deferred Gain is permanently excluded from recognition, and if the investor has held the QOF investment for at least seven years on the Gain Inclusion Date, an additional 5 percent of the Deferred Gain is permanently excluded from recognition. Third, if the investor has held the QOF investment for at least 10 years, the investor can elect to exclude all appreciation in the QOF investment (above the Deferred Gain, which must be recognized no later than 2026) when such interest in the QOF is sold, so long as the investment has otherwise met the Qualified Opportunity Zone ("QOZ") regime requirements. If the QOF instead sells its QOZ property or a QOZ business sells assets after an investor meets such 10-year holding period, the investor may likewise elect to exclude all gain recognized in respect of such sale (subject to an exclusion for certain inventory items).

Status: Long-awaited QOF final regulations were released on December 19, 2019. Although the final regulations are helpful in clarifying certain areas of uncertainty, there are still some unanswered questions and areas of ambiguity. The rules are complex and some uncertainty persists; accordingly, it remains essential to form QOFs and to make QOF investments only after careful planning (including a thorough assessment of nontax legal and business risks) and discussions with tax counsel.

The Lowenstein Sandler LLP Tax Group alert discussing QOFs is available here.

Privacy and Cybersecurity Updates

Synopsis: The relevant laws, regulations, and regulatory guidance with respect to privacy and cybersecurity are continuing to evolve. Firms should reevaluate their practices, policies, and procedures in light of the new California Consumer Privacy Act ("CCPA") and recent OCIE guidance on privacy, cybersecurity, and resiliency.

Status: The CCPA, effective on January 1, 2020, is the first comprehensive data protection law in the United States. In contrast to most U.S. data protection laws that apply only to certain industries, the CCPA regulates organizations in *any industry* that meet the statutory requirements. No *industry* is exempt from the CCPA, but *specific categories of data* may be exempt. Specifically with respect to financial services, including registered investment advisers, nonpublic personal information processed by a financial institution under the Gramm-Leach-Bliley Act ("GLBA") is not regulated by the CCPA. All other personal information of California residents, households, and devices processed by the investment adviser is governed by the CCPA, including personal information pertaining to employees, business contacts, and online activities. As a result, information available to a registered investment adviser and protected by the GLBA covers most *but not all* information that is protected by the CCPA. While the

General Data Protection Regulation ("GDPR") clearly influenced the CCPA, there are substantial differences between them. Investment advisers should be able to leverage some of the work done for GLBA and GDPR compliance, but compliance with the CCPA imposes new and different requirements.

In a May 23, 2019, risk alert relating to data storage, OCIE highlighted a number of compliance concerns arising from misconfigured network storage solutions, inadequate oversight of vendor-provided network storage solutions, and insufficient data classification policies and procedures. OCIE encourages registered broker-dealers and investment advisers to review their practices, policies, and procedures with respect to the storage of electronic customer information and to actively oversee outside vendors in this area.

In an April 16, 2019, risk alert relating to privacy notices and safeguard policies, OCIE highlighted that a number of firms are failing to provide privacy notices and failing to implement and enforce policies and procedures as required under the Safeguards Rule of Regulation S-P (noting that certain policies were found to merely restate the Safeguards Rule or found to include blanks that were not completed by the firm). Inadequacies were noted in areas such as personal devices, electronic communications, training and monitoring, unsecure networks, outside vendors, inventories of personally identifiable information, incident response plans, unsecure physical locations, shared login credentials, and removal of departed employee access.

On January 27, 2020, OCIE released a 13-page statement setting forth detailed observations on cybersecurity and operational resiliency. The statement discusses governance and risk management, access rights and controls, data loss prevention, mobile security, incident response and resiliency, vendor management, and training and awareness. Firms are urged to review their practices, policies, and procedures in these areas and implement some or all of OCIE's suggested measures to make the organization more secure.

OCIE's risk alert on data storage is available here. OCIE's risk alert on privacy and safeguard policies is available here. OCIE's statement on cybersecurity and resiliency is available here.

Supervision of Persons With Disciplinary History

Synopsis: In a July 23, 2019, risk alert, OCIE highlighted a number of compliance concerns observed during examinations of investment advisers employing supervised persons with a disciplinary history.

Status: Among other issues, OCIE noted that nearly half of firms failed to provide adequate information concerning disciplinary events through: (i) reliance on supervised persons to self-report; (ii) inadequate or misleading information; or (iii) failure to timely update and deliver disclosure documents to clients in respect of new disciplinary events. OCIE noted that compliance programs were overly reliant on self-reporting by supervised persons of their own disciplinary events or recent bankruptcies (or lack thereof). Beyond supervised persons with disciplinary histories, OCIE identified a number of other areas for improvement in relation to compliance, supervision, and disclosure of conflicts of interest.

OCIE's risk alert on supervision of persons with disciplinary history is available here.

COMPLIANCE CHECKLISTS

PRIVATE INVESTMENT FUNDS AND THEIR ADVISERS

- ☐ **Conduct periodic review of compliance policies.**
- ☐ **Provide/collect new issues certifications (taking into account 2019 changes to FINRA Rules 5130 and 5131) regarding whether funds/investors are "restricted persons."**
- ☐ **Conduct periodic review and update of offering documents.**
- ☐ **Consult counsel regarding annual Form D amendments and blue-sky and local securities matters in connection with offers or sales.**
- ☐ **Make certain Schedule 13G filings by February 14, 2020.**
- ☐ **File Schedule 13G year-end amendments by February 14, 2020.**
- ☐ **File Schedule 13H year-end amendments by February 14, 2020.**
- ☐ **File Form 13F for fourth quarter of 2019 by February 14, 2020.**
- ☐ **File Form PF quarterly updates and annual updates.**
- ☐ **Conduct periodic review of Section 13 and Section 16 filings**
- ☐ **Conduct periodic review of BEA and TIC forms.**
- ☐ **Monitor compliance with 25 percent ERISA limitation with respect to benefit plan investors.**
- ☐ **Prepare annual VCOC Certification (if required) for benefit plan investors.**
- ☐ **Prepare Form 5500 Schedule C fee disclosures for ERISA plan investors.**
- ☐ **Prepare year-end audits and distribute financial statements as appropriate.**
- ☐ **Collect annual holdings reports and annual certifications from access persons and other personnel.**
- ☐ **Renew "bad actor" questionnaires, and conduct placement agent verifications.**
- ☐ **Conduct annual training of personnel.**
- ☐ **Update risk assessment.**
- ☐ **Conduct periodic anti-money laundering verifications (e.g., OFAC verifications).**
- ☐ **Reevaluate state privacy obligations.**
- ☐ **Distribute privacy notices, if required.**

Discussion:

Compliance Policies. The compliance and operating requirements pertaining to registered investment advisers and unregistered advisers (including exempt reporting advisers) have continued to merge, and more and more unregistered managers are adopting best practices and upgrading their compliance policies to meet the demands of regulators and/or investors. Whether your firm is currently federally registered or will be required to register in the future, you should review your compliance policies periodically to verify that they are adequate and appropriately tailored to your business risks and that your firm is adhering to them.

New Issues Certifications. If you purchase "new issues" (i.e., equity securities issued in an initial public offering), your broker (or, if you are a fund-of-funds that invests indirectly in new issues, the underlying funds) will require that you certify each year as to whether the fund is a "restricted person" within the meaning of FINRA Rules 5130 and 5131. To make the certification, you must determine the status of investors in your fund as either restricted persons or unrestricted persons. Certain amendments to FINRA Rules 5130 and 5131 were made in 2019 as described above. The Lowenstein Sandler LLP

Investment Management Group alert analyzing FINRA'S amendments to FINRA Rules 5130 and 5131 is available here.

Offering Documents. Offering documents should be reviewed from time to time to verify that they: (i) contain a current, complete, and accurate description of the fund's strategy, management, and soft-dollar and brokerage practices; (ii) comply with current laws and regulations; and (iii) reflect current disclosure best practices.

Form D Amendments and Blue Sky and Local Securities Matters. You should continue to inform counsel of all offers or sales of fund interests. Ongoing offerings may necessitate an amendment to a private fund's Form D (typically required on an annual basis on or before the first anniversary of the most recent notice previously filed). Additionally, offers to U.S. persons may trigger filing obligations in a given investor's state of residence, while offers to foreign persons may require filings in the country of an investor's residence.

Beneficial Ownership Reporting Requirements. Certain Schedule 13G filings pursuant to Sections 13d-1(b) and 13d-1(d) of the Securities Exchange Act of 1934 (as amended, the "Exchange Act") are required to be filed by February 14, 2020. If you have filed Schedule 13G previously and the information reflected in the schedule is different as of December 31, 2019, from that previously reported, you are generally required to have amended the schedule by February 14, 2020. Form 5 must be filed within 45 days of the end of the issuer's fiscal year (February 14, 2020, for issuers with a December 31, 2019, fiscal year-end). Year-end serves as a convenient time to confirm that all relevant Section 13 and Section 16 filings are current and complete.

BEA and TIC Forms. The beginning of the calendar year is a good time to conduct a review of the applicable U.S. Bureau of Economic Analysis ("BEA") and Treasury International Capital ("TIC") forms and filing requirements applicable to your firm. TIC forms may be due on a monthly, quarterly, or annual basis and are subject to frequent updates. BEA forms may be due, as applicable, within 45 days of a relevant transaction or quarterly, annually, or every five years. The BEA provides a webpage offering specific guidance to private funds here. The U.S. Treasury Department provides a resource center with respect to TIC Forms and Instructions here.

Form 13H. Section 13(h) of the Exchange Act established a reporting system and filing requirements for "large traders," i.e., persons effecting transactions in certain securities in amounts equal to 2 million shares or $20 million (determined by fair market value of the shares) in one calendar day, or 20 million shares or $200 million in one calendar month. Persons meeting these thresholds must file Form 13H no later than 10 days after the identifying activity level is reached. Amended filings must be effected promptly after the end of a calendar quarter during which any of the information contained in Form 13H becomes outdated or inaccurate. Large traders may file amended filings more often than quarterly but are not required to do so. Annual amendments (regardless of the number of amended filings previously effected) are due within 45 days of the end of each calendar year. Persons may now satisfy both the amended fourth-quarter filing and the annual update to Form 13H, as long as such filing is made within the period permitted for the fourth-quarter amendment (i.e., promptly after the fourth quarter's end).

Form 13F. Section 13(f) of the Exchange Act requires "institutional investment managers" with investment discretion over $100 million or more of certain equity securities to file quarterly reports on Form 13F. Form 13F must be filed within 45 days of the end of each calendar quarter. An initial Form 13F must be filed at the end of the first year in which an institutional investment manager exceeds the $100 million threshold. To the extent that you have a Form 13F filing obligation, you were required to file your Form 13F for the fourth quarter of 2019 by February 14, 2020.

Form PF. Many smaller private advisors and large private equity advisors will be required to file an annual update to Form PF by April 29, 2020 (120 days after the end of their fiscal year). Quarterly updates to Form PF are required of large hedge fund advisors (by February 29, 2020, or 60 days after the end of their fiscal quarter) and large liquidity fund advisors (by January 15, 2020, or 15 days after the end of their fiscal quarter). Please be advised that the Investment Adviser Registration Depository ("IARD)" system (and the Private Fund Reporting Depository subsystem of the IARD) will be available on Saturday, February 29, 2019, from 8 a.m. to 6 p.m. Eastern time to accommodate Form PF filings.

Monitor Compliance With 25 Percent ERISA Limitation on Benefit Plan Investors. If the aggregate amount invested in a fund by "benefit plan investors" (e.g., employee benefit plans, individual retirement accounts, Keogh plans and entities–the underlying assets of which include "plan assets"–but excluding governmental plans, foreign plans, and certain church plans) equals 25 percent or more of the total value of any class of equity interests in the fund (excluding investments by the fund's managers who are not benefit plan investors), the fund will generally be deemed to hold plan assets subject to various ERISA requirements and prohibitions, unless the venture capital operating company ("VCOC") exception (described below) or another regulatory exception applies. Accordingly, many funds (particularly those that do not qualify as VCOCs, such as hedge funds) limit equity participation by benefit plan investors to less than 25 percent. If you sponsor such a fund, you should continuously monitor (i.e., upon subscriptions, capital calls, redemptions, transfers) the level of investments by benefit plan investors to ensure the 25 percent threshold is not exceeded.

Annual VCOC Certification. Prior to investing in a venture fund or a private equity fund, ERISA plan investors often require the fund to provide an annual VCOC certification stating that the fund qualifies as a VCOC. A venture fund or a private equity fund that qualifies as a VCOC will not be deemed to hold plan assets subject to ERISA, even if equity participation by benefit plan investors exceeds the 25 percent threshold (described above). In general, a fund will qualify as a VCOC if: (i) at any time during the fund's annual valuation period, at least 50 percent of the fund's assets (other than short-term investments pending long-term commitment or distribution to investors), valued at cost, are invested in venture capital investments in operating companies for which the fund has management rights; and (ii) the fund, in the ordinary course of its business, actually exercises substantial management rights with respect to one or more of the operating companies in which it invests on an annual basis.

FORM 5500 Schedule C Fee Disclosures. Funds that have ERISA plan investors (including funds that do not allow equity participation by benefit plan investors to exceed the 25 percent threshold (described above) and thus are not subject to ERISA), excluding VCOCs and other entities treated as operating companies, are required to provide plan administrators of their ERISA plan investors with certain fee-related information that is necessary for the completion of Schedule C to the plan's annual report on Form 5500 in advance of the filing deadline for the annual report. The Lowenstein Sandler LLP alert analyzing the Form 5500 Schedule C rules is available here.

Year-End Audit. Now is the time to begin all necessary year-end audits so that funds can distribute financials to investors on a timely basis as required by relevant governing documents and, in certain instances, as required to comply with the custody rule under the Advisers Act and/or CFTC requirements.

Annual Holdings Reports and Annual Certifications. The beginning of the calendar year is a good time for investment advisers to have all "access persons" provide their annual holdings reports regarding securities ownership required pursuant to Rule 204A-1 of the Advisers Act. It is also a good time to have all personnel provide their annual certifications of compliance with firm policies and conflict-of-interest questionnaires.

"Bad Actor" Questionnaires and Placement Agent Verifications. The beginning of the calendar year is a good time to have certain personnel and service providers (e.g., directors of offshore private funds) recertify their status with respect to the SEC's "bad actor" rules in order to rely on the private placement exemption under Rule 506. This bad actor certification is often combined with the annual certification of compliance with firm policies discussed above. It is also a good time to have placement agents recertify their status with respect to such rules and certain other disciplinary matters.

Conduct Annual Training of Personnel. As a best practice under the Advisers Act, investment advisers should hold annual training sessions with existing employees to remind them of their obligations under the firm's compliance manual and code of ethics.

Update Risk Assessment. As a best practice under the Advisers Act, investment advisers should annually reevaluate their "risk assessment" (i.e., evaluation of how the firm's activities, arrangements, affiliations, client base, service providers, conflicts of interest, and other business factors may cause violations of the Advisers Act or the appearance of impropriety) to determine that new, evolving, or resurgent risks are adequately addressed.

Periodic Anti-Money Laundering Verifications. Private investment funds and their advisors have ongoing anti-money laundering compliance obligations that necessitate periodic verifications, the frequency of which depend on such funds' and advisers' operations. The beginning of the calendar year is a good time to assess such obligations and to conduct renewed verifications such as comparing investor bases with the U.S. Treasury Department's Office of Foreign Assets Control lists.

Privacy Notices. In accordance with applicable federal law, investment advisers and investment funds must have a privacy policy in place. In addition to being provided at the time of initial subscription, privacy notices must generally be distributed at least annually, and more frequently if there are any changes to the policy/notice. An exception provides that annual notice is not required where an adviser or fund (i) only shares non-public personal information ("NPPI") with nonaffiliated third parties in a manner that does not require an opt-out right be provided; and (ii) has not changed its policies and practices with regard to disclosing NPPI since its most recent distribution of its privacy notice. Now is an opportune time for advisers and funds to determine whether they can rely on this exception and to review their privacy notices in light of the recent OCIE risk alert on privacy notices, discussed above. We believe that the best time for the annual distribution of the notice, if required, is with a fund's annual financial statements and/or tax reports. Additionally, as discussed above, California's recently enacted CCPA (and other state privacy laws and regulations) may subject investment advisers and investment funds to additional and/or more stringent privacy requirements.

REGISTERED INVESTMENT ADVISERS AND EXEMPT REPORTING ADVISERS (WHERE INDICATED)

- ☐ **Prepare annual updating amendments to Form ADV (for registered investment advisers and certain "Exempt Reporting Advisers").**
- ☐ **Update investment policy statements and investment management agreements, taking into account 2019 changes to FINRA Rules 5130 and 5131 (relating to new issue distribution restrictions).**
- ☐ **Deliver Form ADV Part 2A (or portions thereof) to clients and fund investors (for registered investment advisers).**
- ☐ **Comply with state annual filing requirements.**
- ☐ **Conduct periodic review of compliance policies and code of ethics.**
- ☐ **Comply with custody rule annual surprise examination.**
- ☐ **File Form 13F for fourth quarter of 2019 by February 14, 2020.**
- ☐ **Distribute privacy notices, if required.**
- ☐ **Prepare Form 5500 Schedule C fee disclosures for ERISA plan accounts.**
- ☐ **Comply with ERISA Section 408(b)(2) fee disclosure requirements for Covered Plans.**
- ☐ **Conduct periodic vendor due diligence updates, including in respect of proxy advisory firms.**

Discussion:

Annual Updating Amendments to Form ADV. An investment adviser that (i) is registered with the SEC; or (ii) is considered an "Exempt Reporting Adviser" (i.e., an investment adviser relying on the private fund adviser exemption or the venture capital adviser exemption), in each case as of December 31, 2019 (and with a December 31, 2019, fiscal year-end), must file an annual updating amendment of items on the form by March 30, 2020.

Updates in Respect of New Issue Distribution Restrictions. Certain amendments to FINRA Rules 5130 and 5131 were made in 2019 as described above. Investment advisers should update their investment policy statements and investment management agreements, taking into account 2019 changes to FINRA Rules 5130 and 5131. The Lowenstein Sandler LLP Investment Management Group alert analyzing FINRA'S amendments to FINRA Rules 5130 and 5131 is available here.

Deliver Form ADV Part 2. An investment adviser that is registered with the SEC and whose Form ADV Part 2A has materially changed since such adviser's last annual amendment must deliver either an amended Part 2A (which must include a summary of such material changes) or a summary of such material changes (which must include an offer to provide a copy of the amended Part 2A). Although such delivery requirements expressly apply only to "clients" (as defined in federal securities laws), we recommend that advisers to private funds deliver such items to their fund investors. For advisers with a December 31, 2019, fiscal year-end, such items must be delivered by April 29, 2020.

State Filing Requirements. Applicable state law may require a federally registered investment adviser to make notice filings and to pay fees in the state if he or she has clients or a place of business therein. Laws vary significantly from state to state. There also may be certain licensing or qualification requirements for representatives of investment advisers. Please contact counsel with any state-specific questions.

Compliance Policies and Code of Ethics. Federally registered investment advisers must adopt and maintain comprehensive compliance policies and a code of ethics and also must appoint a chief compliance officer. If you have not already done so, please contact counsel immediately for assistance in creating and/or documenting compliance procedures appropriately tailored to your business. In addition, compliance policies and procedures must be reviewed by the advisor at least annually. The compliance policies and procedures review should focus on an evaluation of the effectiveness of the policies and procedures in light of current risks and the need for revisions as a result of: (i) any compliance issues that arose during the prior year; (ii) any changes in the business activities of the investment adviser; and/or (iii) any regulatory changes. We recommend that this review be conducted relatively early in the year or staggered throughout the year so that it does not interfere with other time-sensitive activities when quarter-end or year-end matters are pressing. Policies that are materially changed as a result of such review should be redistributed to all appropriate personnel. In addition, Item 11 of Form ADV Part 2A must contain a current description of the code of ethics and a statement that the investment adviser will provide the code of ethics to any current or prospective client upon request.

Custody Rule Annual Surprise Examination. With certain limited exceptions, where the adviser (or its related person) possesses or may possess client funds and securities, the adviser is required to undergo an annual surprise examination by an independent public accountant.

Form 5500 Schedule C Fee Disclosures. Advisers managing ERISA plan accounts are required to disclose certain fee-related information necessary for plan administrators to complete Schedule C to the plan's annual report on Form 5500 in advance of the date such annual report is required to be filed. The Lowenstein Sandler LLP alert analyzing the Form 5500 Schedule C rules is available here.

Compliance With ERISA Section 408(b)(2) Fee Disclosure Requirements. Advisers providing services directly to an ERISA-covered defined contribution or defined benefit plan as either a fiduciary or a registered investment adviser (as well as fiduciary services to a first-tier ERISA "plan asset" fund in which a covered plan has a direct investment, brokerage and record-keeping services to certain participant-directed plans to which investment alternatives are made available, and certain other services) are generally required to make detailed fee disclosures to a plan fiduciary in advance of the date the underlying contract or arrangement is entered into, extended, or renewed. Additionally, changes to such required fee disclosures must be disclosed as soon as practicable, but in no event more than 60 days from the date on which the adviser becomes informed of such change. Advisers providing such services should monitor ongoing compliance with the ERISA Section 408(b)(2) disclosure requirements. The Lowenstein Sandler LLP alert analyzing the Section 408(b)(2) Fee Disclosure Requirements is available here.

Vendor Due Diligence Updates. As part of an effective third-party risk management program, advisers are encouraged to implement an effective due diligence process with respect to service providers utilized by the adviser, consisting of both an initial due diligence assessment and periodic reviews thereafter. Such periodic reviews may include tailored certifications from the vendor in light of the services provided by each such vendor; review of the vendor's regulatory history, public filings, registrations, and licenses (as applicable); a review of the vendor's financial statements; and (as necessary) conference calls and on-site visits. Advisers should document the due diligence process and results.

COMMODITY POOL OPERATORS AND COMMODITY TRADING ADVISORS

- ☐ **Registered CPOs and CTAs must conduct annual regulatory compliance reviews and complete certain regulatory requirements, which include preparation of annual questionnaires and annual registration updates (applies to registered CPOs and CTAs).**
- ☐ **Prepare and file certain portions of Form CPO-PQR by March 2, 2020 (applies to CPOs with $1.5 billion or more in AUM), or March 31, 2020 (applies to other CPOs).**
- ☐ **Prepare and file certain portions of Form CTA-PR by February 14, 2020.**
- ☐ **Annual affirmation of CPO registration exemption under Sections 4.5, 4.13(a)(1)-(3), or 4.13(a)(5), or exemption from CTA registration under Section 4.14(a)(8), by February 29, 2020.**
- ☐ **Review CPO delegations in connection with annual pool financial statement filings.**

Discussion:

Annual Compliance Reviews/Regulatory Requirements. Registered CPOs and CTAs must conduct annual compliance reviews. These reviews and requirements include: (i) the preparation and filing with the NFA of Annual Questionnaires and Annual Registration Updates within 30 days of the anniversary date of their registration; (ii) completion of the NFA's Self-Examination Checklist; (iii) sending Privacy Policies to every current customer, client, and pool participant; (iv) testing disaster recovery plans and making necessary updates; (v) providing ethics training to staff, and inspecting the operations of branch offices; (vi) for registered CPOs, preparation of Pool Quarterly Reports within 45 days after the end of the year (and within 45 days after the end of each quarter); and (vii) for registered CTAs that are NFA Members, the filing of Form CTA-PR, required within 45 days after the end of the year (and within 45 days after the end of each quarter). Finally, unless the applicable fund(s) qualify for an exemption, registered CPOs and CTAs must update their disclosure documents periodically, as they may not use any document dated more than 12 months prior to the date of its intended use. Disclosure documents that are materially inaccurate or incomplete must be promptly corrected, and the correction must be promptly distributed to pool participants. The NFA's Notice to Members regarding these regulatory compliance matters is available here.

Prepare and File Portions of Form CPO-PQR. CPOs with AUM exceeding $1.5 billion must have filed Schedules

A, B, and C by March 2, 2020, and other CPOs must file Schedule A (and Schedule B if AUM exceeds $150 million) by March 31, 2020.

Prepare and File Portions of Form CTA-PR. CTAs are required to have completed Form CTA-PR by February 14, 2020 (45 days after the end of the calendar quarter for CTAs who are NFA Members, and 45 days after the end of the calendar year for other CTAs).

Annual Affirmation of CPO or CTA Exemption. Each person who has filed a notice of exemption from CPO registration under Sections 4.5, 4.13(a)(1)-(3), or 4.13(a)(5), or exemption from CTA registration under 4.14(a)(8), must have affirmed such notice of exemption by February 29, 2020, through the NFA's exemption system.

Review of CPO Delegations. All CPO delegation agreements entered into by registered CPOs must comply with specific criteria set forth by the CFTC and must be retained as part of the relevant CPO's records. As part of their annual pool financial statement filings through the NFA website, CPOs should ensure that all necessary CPO delegations are in place and appropriately documented.

RECENT PUBLICATIONS AND COMMENTARY

Below are links to recent articles and publications featuring or authored by members of the Investment Management Group.

CLIENT ALERTS AND NEWSLETTERS

- **Key Takeaways From SEC's Reg. BI Frequently Asked Questions**
  Investment Management Client Alert
  Ethan L. Silver, Lauren A. Schwartz, Alexander D. Zozos
  January 27, 2020

- **FINRA 2020 Risk Monitoring and Examination Priorities Letter**
  Investment Management Client Alert
  Ethan L. Silver, William Brannan, Brian Nistler, Lauren A. Schwartz, Alexander D. Zozos
  January 22, 2020

- **SEC's OCIE Releases 2020 Examination Priorities for Investment Advisers, Broker-Dealers, and Other Financial Industry Professionals**
  Investment Management Client Alert
  Ethan L. Silver, Scott H. Moss, David L. Goret, Lauren A. Schwartz, Brian Nistler
  January 16, 2020

- **FINRA Amends New Issue Rules 5130 and 5131**
  Investment Management Client Alert
  Scott H. Moss, Eileen Overbaugh, Alexander D. Zozos
  January 15, 2020

- **FINRA to Broker-Dealers Gearing Up for Regulation BI, "Don't Panic–Prepare!"**
  Investment Management Client Alert
  Ethan L. Silver, Lauren A. Schwartz, Alexander D. Zozos
  January 9, 2020

- **The SEC Division of Enforcement Publishes 2019 Results**
  Lowenstein Sandler Client Alert
  H. Gregory Baker, David L. Goret, Rachel Maimin, Scott H. Moss, Alexandra S. Droz
  November 13, 2019

- **SEC Seeks to Modernize Laws of Attraction for Investment Advisers by Updating Advertising and Cash Solicitation Rules**
  Investment Management Client Alert
  Scott H. Moss, Scott Balterman, Lauren A. Schwartz, Alexander D. Zozos
  November 12, 2019

- **FINRA Provides Guidance on Regulation Best Interest and Form CRS**
  Investment Management Client Alert
  Ethan L. Silver, Lauren A. Schwartz, Alexander D. Zozos
  October 17, 2019

- **SEC Identifies Common Principal and Agency Cross Trading Compliance Deficiencies**
  Investment Management Client Alert
  Scott H. Moss, Robert J. Menendez, Gina M. Russoniello
  September 18, 2019

- **Is the Internet Public? A Review of the Ninth Circuit's Decision in hiQ Labs, Inc. v. LinkedIn Corporation**
  Investment Management Client Alert
  Peter D. Greene, Benjamin Kozinn, Robert J. Menendez
  September 16, 2019

- **SEC Further Clarifies Proxy Voting Responsibilities of Investment Advisers**
  Investment Management Client Alert
  Scott H. Moss, David L. Goret, Ethan L. Silver, Lauren A. Schwartz
  September 6, 2019

- **SEC Clarifies Federal Fiduciary Duties of Investment Advisers**
  Investment Management Client Alert
  Scott H. Moss, Manas Kumar
  July 2, 2019

- **SEC Settlement With Corinthian Capital Reflects Continued Scrutiny of Private Equity Firms and Other Fund Managers**
  Private Equity and Investment Management Client Alert
  H. Gregory Baker, Scott H. Moss
  May 16, 2019

UPCOMING EVENTS

Below is information regarding upcoming events sponsored by or featuring members of the Investment Management Group. For more information regarding any of these events, please contact events@lowenstein.com.

Opal Family Office Winter Forum 2020
March 3, 2020
New York Athletic Club, New York, NY
Lesley P. Adamo, "Opportunity Zones & the Impact of Tax Reform on Real Estate Strategies: Market Level Update"
Marie T. DeFalco, "Direct vs. Co-Investment vs. Commingled Funds"
Max Karpel

100 Women in Finance
March 10, 2020
New York, NY
Eileen Overbaugh

MFA Legal & Compliance Conference 2020
April 2, 2020
The Plaza, New York, NY
Peter D. Greene, Scott H. Moss

GAIM: Ops Cayman 2020
April 19 - 22, 2020
Ritz-Carlton, Grand Cayman
Benjamin Kozinn, Max Karpel, Eileen Overbaugh

Israeli Hedge Funds Association 8th Annual Conference
May 26, 2020
Tel Aviv, Israel
Max Karpel, "Global Regulatory Environment"

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