

# Regulatory and Enforcement Alert

## The SEC Intends to Proceed Full Steam Ahead With Its Extensive Rulemaking Agenda for Investment Advisers, Private Funds and Registered Funds

June 15, 2023

The Office of Information and Regulatory Affairs recently released the SEC's Spring 2023 [Unified Agenda of Regulatory and Deregulatory Actions](#) (the "Agenda"), which identifies the most significant regulatory actions that the SEC reasonably expects to issue in proposed or final form and the broad targeted time frame to issue such rules. As detailed below, the Agenda indicates that the SEC expects to continue carrying out its expansive rulemaking agenda at a blistering pace with respect to investment advisers, private funds and registered funds, with several major rule proposals slated for adoption in the second half of 2023.

The target time frames in the Agenda generally reflect the SEC's reasonable estimate of when such action may occur. However, the proposal or adoption of a rulemaking item listed on the Agenda may occur earlier or later than the target date provided on the Agenda, and may not occur at all. Nonetheless, the Agenda provides useful information concerning the SEC's plans and priorities and the broad timing of potential rulemaking actions.

As compared with the two most recent published versions of the SEC's regulatory agendas, the Agenda has a larger number of rules in the Final Rule Stage and a smaller number of rules in the Proposed Rule Stage, both generally and with respect to rules focused on investment advisers and funds. This appears to reflect that, approximately two years into Chair Gensler's tenure, the SEC is generally shifting its emphasis from proposing additional rules to taking final action on previously proposed rules.

Below is a breakdown of the target time frames for final action on previously proposed rules concerning investment advisers and funds, and descriptions of a few notable contemplated rule proposals concerning investment advisers and funds.

### Previously Proposed Rules—Final Action Contemplated for the Fourth Quarter of 2023<sup>1</sup>

- **Private Funds Rule:** As detailed in a prior [Simpson Thacher publication](#), this sweeping proposal targeting private equity and other private funds would significantly expand the disclosure of standardized fee and expense information, and require registered private fund advisers to obtain an annual audit for each

<sup>1</sup> For these rule proposals, the targeted Final Action date in the Agenda is October 2023, which we view as indicating expected adoption of these proposals in the fourth quarter of 2023.

private fund it advises. This proposal would also broadly prohibit certain practices in the private funds industry, including prohibiting: a fund manager from being indemnified in cases of ordinary negligence, the negotiation of preferential terms for certain investors via side-letters unless these terms are disclosed to current and prospective investors, and a private fund adviser and its related persons from granting preferential redemption rights to certain investors if the adviser reasonably expects that redemption to have a material negative effect on other fund investors. Finally, this proposal would require that investors be provided a fairness opinion for adviser-led secondary transactions. We expect that a final vote for the Private Funds Rule will occur in 2023.

- ***Safeguarding Rule:*** As detailed in a prior [Simpson Thacher publication](#), this dramatic set of amendments to the Advisers Act custody rule would require registered investment advisers to enter into written agreements with clients' qualified custodians that contain certain assurances, and require that qualified custodians have possession or control of the client assets for which they have custody. In addition, the proposal would require, for privately-offered securities not maintained at a qualified custodian, that the investment adviser document that such securities cannot be maintained at a qualified custodian and that an independent public accountant promptly verify any purchase, sale or transfer of such a security. The proposal would expand the custody rule to apply to all client assets, including assets such as digital assets and real estate that are not securities. In our view, the SEC's target for final action on this proposal in the fourth quarter of 2023 is very ambitious, given that this proposal did not receive unanimous support from the SEC's Commissioners, leaves several substantial questions unanswered, and was only proposed earlier this year.
- ***Form PF; Reporting Requirements for All Filers and Large Hedge Fund Advisers:*** This [proposal](#), which was made jointly by the SEC and the CFTC, would require all Form PF filers to provide additional and more granular information concerning master-feeder arrangements, parallel funds and investments in funds that are not private funds. This proposal would also impose additional reporting obligations on Large Hedge Fund Advisers. These proposed amendments are separate from the Form PF amendments for Large Hedge Fund Advisers and Large Private Equity Fund Advisers that the SEC [adopted](#) in May 2023.
- ***Enhanced Disclosures by Certain Investment Advisers and Investment Companies About Environmental, Social and Governance Investment Practices and Investment Company Names:*** The [proposal](#) for enhanced disclosure would require investment companies and investment advisers to provide more specific disclosures in fund filings and investment adviser brochures regarding the ESG strategies that they pursue and the specific ESG impact(s) they seek to achieve, and require additional disclosures by funds that use proxy voting or other issuer engagements to implement their ESG strategy. The fund names rule [proposal](#) would, among other measures, expand the current requirement of the names rule for certain registered funds to adopt a policy related to the 80 percent investment requirement.

- **Cybersecurity Risk Management for Investment Advisers, Investment Companies and Business Development Companies:** This [proposed](#) rule would require SEC-registered advisers and funds to adopt and implement written policies and procedures that are reasonably designed to address cybersecurity risks and to provide additional disclosures related to cybersecurity risks and incidents in investment adviser brochures and fund filings. It would also require SEC-registered investment advisers to report significant cybersecurity incidents to the SEC within 48 hours of the incident’s occurrence.
- **Open-End Liquidity Risk Management Programs and Swing Pricing:** These [proposed](#) amendments would require most open-end funds to use swing pricing to adjust their NAV per share, in order to pass on costs stemming from shareholder purchase or redemption activity to the shareholders engaged in the activity. The proposed amendments would also require additional disclosures on Forms N-PORT, N-1A, N-CEN for certain registered investment companies, and require more frequent reporting of monthly portfolio holdings and information about liquidity risk management and swing pricing to the SEC and the public.
- **Modernization of Beneficial Ownership Reporting:** This [proposal](#) would accelerate the filing deadlines for Schedules 13D and 13G beneficial ownership reports, expand the application of Regulation 13D and 13G to certain derivative securities, expand the circumstances under which two or more persons will be deemed to have formed a “group” that would be subject to beneficial ownership reporting obligations, and require that Schedules 13D and 13G be filed using a structured, machine-readable data language.

## Previously Proposed Rules—Final Action Contemplated for Early 2024<sup>2</sup>

- **Outsourcing by Investment Advisers:** This [proposal](#) would require registered investment advisers to conduct due diligence before outsourcing various functions, monitor and reassess service providers’ performance, and make and keep books and records related to such due diligence and monitoring. The proposal would also require investment advisers to conduct due diligence and monitoring of third-party record-keepers and to obtain certain assurances from these third-party record-keepers. Moreover, this proposal would amend Form ADV to collect census-type information about investments advisers’ use of service providers. The expansive scope of this proposal generated a considerable number of comments in opposition.
- **Regulation S-P:** As detailed in a prior [Simpson Thacher publication](#), this proposal would amend regulation S-P to create a federal minimum standard for covered institutions (broker-dealers, registered investment companies including BDCs, registered investment advisers and transfer agents) for preventing and responding to data breaches, including providing notice to certain affected stakeholders, and require covered institutions’ contracts with service providers to include measures to protect against data breaches.

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<sup>2</sup> For these rule proposals, the targeted Final Action date in the Agenda is April 2024.

## Contemplated Rule Proposals

In addition to the previously proposed rules discussed above, the Agenda identifies the following contemplated rule proposals that we believe, based on the limited description provided in the agenda, are potentially noteworthy to investment advisers and funds:

- ***Prohibition of Conflicted Practices for Investment Advisers and Broker-Dealers That Use Certain Covered Technologies:*** The Division of Investment Management and the Divisions of Trading and Markets are considering recommending separate proposed rules related to investment advisers' and broker-dealers' conflicts of interest in the use of predictive data analytics, artificial intelligence, machine learning and similar technologies in connection with certain investor interactions. These contemplated proposals appear to respond to the recent significant advancements in and potential use of artificial intelligence and technology in financial markets and the economy generally. Both of these contemplated rule proposals are targeted for proposal in the fourth quarter of 2023.
- ***Fund Fee Disclosure and Reform:*** The Division of Investment Management is considering recommending that the Commission propose changes to regulatory requirements relating to registered investment companies' fees and fee disclosure. This contemplated rule proposal is targeted for proposal in the first half of 2024.

The SEC does not appear to be relenting in its regulatory agenda with respect to investment advisers, private funds and registered funds, and the second half of 2023 is expected to be active and consequential for the asset management industry.

For additional information concerning these SEC rule proposals and/or the SEC's agenda generally, please contact one of the following members of the Firm's [Funds Regulatory and Investigations Practice](#).

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