Jefferies

ELECTRONIC & PROGRAM TRADING

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U.S. Market Structure Update

Here's what's happening…

UPDATED: The SEC's Proposals All in One Place... Here's What You Need to Know

In 2022 alone, the SEC has released close to 20 major proposals, and more are expected in the weeks and months to come. To help stay up to date and keep track of them all, we've compiled overviews of each proposal (most of them) with links to additional information and put them into a single document. ***This document is an update to our first note, which was published on May 11, 2022****.*

All summaries were directly sourced from the information and language published by the SEC as well as third-party websites and firms that publish on the topic of securities regulation. Please note we do not opine on the proposals in any way as each one is extensive and could affect different firms in a variety of ways. Thus, certain elements potentially relevant to you and your firm may not be included here.

Our intention is for this document to be a resource for you and your firm, so please feel free to circulate it to others who may find it useful.

Jefferies Global Market Structure

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Amendments to Form PF to Require Current Reporting and Amend Reporting Requirements for Large Private Equity Advisers and Large Liquidity Fund Advisers

Amendments to Form PF, the confidential reporting form for certain SEC-registered investment advisers to private funds, would:

- ❖ Require new current reporting of certain events for large hedge fund advisers and advisers to private equity funds
- ❖ Decrease the reporting threshold for large private equity advisers
- ❖ Revise reporting requirements for large private equity advisers and large liquidity fund advisers

What does the proposal do?

The proposal would make three primary changes to Form PF.

1) **NEW CURRENT REPORTING FOR LARGE HEDGE FUND ADVISERS AND ADVISERS TO PRIVATE EQUITY FUNDS**: The proposal is designed to allow the SEC and FSOC to receive more timely information about certain events that may signal distress at qualifying hedge funds and private equity funds or market instability.

   - The proposal would require **large hedge fund advisers** to file current reports within one business day of the occurrence of one or more reporting events with respect to their qualifying hedge funds pertaining to certain extraordinary investment losses, significant margin and counterparty default events, material changes in prime broker relationships, changes in unencumbered cash, operations events, and events associated with withdrawals and redemptions

   - According to a recent article published by The National Law Review, under the proposed amendments, **large hedge fund advisers** would be required to report the following events within one business day of their occurrence:

     i. Extraordinary investment losses, which the SEC defines as a hedge fund's loss of 20 percent or more of its most recent net asset value over a rolling 10-business-day period[7]

     ii. Significant margin and default events, such as (i) a significant increase in a hedge fund's requirements for margin, collateral, or an equivalent (collectively, "margin"),[8] (ii) a fund's margin default or inability to meet a call for margin, and (iii) a counterparty's margin default[9]

     iii. Any material change in the relationship between a hedge fund and a prime broker, such as material changes to the fund's ability to trade or a termination of the prime brokerage relationship[10]

     iv. Declines in a fund's unencumbered cash holdings of at least 20 percent over a rolling 10-business-day period[11]

     v. Any significant disruption or degradation of a fund's key operations, including (i) its investment, trading, valuation, reporting, and risk management capacity, (ii) its compliance with U.S. securities laws and regulations, and (iii) its ability to properly value its assets

     vi. Large withdrawal and redemption requests exceeding 50 percent of a hedge fund's most recent net asset value, netted against subscriptions and other contributions already received from and committed by investors; and

     vii. A fund's inability to satisfy redemptions, or suspensions of redemptions, for more than five consecutive business days

   - The proposal also would require **advisers to private equity funds** to file current reports within one business day of the occurrence of one or more reporting events pertaining to the execution of adviser-led secondary transactions, implementation of general partner or limited partner clawbacks, removal of a fund's general partner, termination of a fund's investment period, or termination of a fund. Based on the above article published by the National Law Review, private equity advisers would be required to report within **one business day**:

     i. The completion of adviser-led secondary transactions, defined as transactions by an adviser or its related persons that offer private fund investors the choice to (i) sell all or a portion of their interests in the private fund, or (ii) convert or exchange a portion of their interests in the fund for interests in another vehicle advised by the adviser

     ii. Any general partner clawback requiring the return of performance-based compensation to the fund

     iii. Any limited partner clawback of 10 percent or more of a fund's aggregate capital commitments

iv. Removal of the adviser as the general partner or similar control person of a fund; and
v. Investors' election to terminate the fund or its investment period

2) **LARGE PRIVATE EQUITY ADVISER REPORTING**: The proposed amendments are designed to assess the extent to which private equity funds, or their advisers may pose systemic risk and to inform the Commission in its regulatory programs for the protection of investors.

- The proposed amendments would reduce the threshold for reporting as a large private equity adviser from **$2 billion to $1.5 billion** in private equity fund assets under management
- According to the National Law Review, the proposal would amend section 4 of Form PF and require large private equity advisers to disclose:
  i. A private equity fund's investment strategies
  ii. Whether any of a fund's portfolio companies was restructured or recapitalized following the fund's investment period
  iii. Whether the fund held an investment in one class, series, or type of securities of a portfolio company while another fund advised by the adviser, or its related persons simultaneously held an investment in a different class, series, or type of securities of the same portfolio company
  iv. Whether the fund borrows or the ability to borrow at the fund-level as an alternative to financing portfolio companies
  v. The percentage of aggregate borrowings of a fund's controlled portfolio companies (CPCs) that is at a floating (rather than fixed) rate; and
  vi. The number of CPCs owned by a fund
- Additionally, the article stated, "If adopted, the proposed amendments would also modify existing portions of section 4 by requiring a private equity adviser to disclose **(i)** more detailed information about the nature of reported events of default, including the party responsible for the event of default; **(ii)** additional identifying information about counterparties providing bridge financing to the advisers' CPCs; and **(iii)** the geographical breakdown of a fund's investments based on a percentage of the fund's net asset value"

3) **LARGE LIQUIDITY FUND ADVISER REPORTING**: The proposal would require large liquidity fund advisers to report substantially the same information as money market funds via Form N-MFP under the recently proposed money market reforms.

- Amendments to section 3 of Form PF would require **large liquidity fund advisers** to report:
  i. Whether the liquidity fund tries to maintain a stable price per share (and if so, what that price is)
  ii. Cash separately from other categories of repo collateral when reporting assets and portfolio information
  iii. The total gross subscriptions and gross redemptions for each month of a fund's reporting period
  iv. Additional information about each of a fund's portfolio securities, including the name of a repo counterparty
  v. Whether a creditor is based in the United States and, if so, whether it is a "U.S. depository institution"
  vi. Whether the fund is established as a cash management vehicle for other funds or accounts managed by the adviser or its affiliates
  vii. Additional information about the fund's beneficial owners
  viii. Information about the portfolio securities that the liquidity fund sold during the reporting period; and
  ix. The fund's weighted average maturity and weighted average life calculated with a dollar-weighted average

Links to Additional Information

- SEC Press Release, Final Proposal, & Fact Sheet: https://www.sec.gov/news/press-release/2022-9
- Proposal Comment Letters: https://www.sec.gov/comments/s7-01-22/s70122.htm
- Copy of Existing Form PF: https://www.sec.gov/about/forms/formpf.pdf
- The National Law Review (Feb. 9, 2022): https://www.natlawreview.com/article/sec-proposes-amendments-to-form-pf-to-increase-oversight-private-funds

Amendments Regarding the Definition of "Exchange" and Alternative Trading Systems (ATSs) That Trade U.S. Treasury and Agency Securities, National Market System (NMS) Stocks, and Other Securities

This proposal would:

- Amend the definition of "Exchange" under the Exchange Act Rule 3b-16; Among other things, this definition would include "non-firm trading interest" versus "orders", and include systems that offer the use of "non-firm trading interest" and the provision of protocols that bring together buyers and sellers for trading any type of security – i.e., "Communication Protocol Systems" (CPSs)
- Expand Regulation ATS for alternative trading systems that trade government securities; Extend Regulation SCI to ATSs that trade government securities
- Amend the Fair Access Rule to require aggregation of the average transaction volumes of ATSs operated by affiliated broker-dealers and
- Expanding disclosure requirements under Form ATS-N for ATSs that trade NMS and certain other securities and switching to an electronic filing system for Form ATS and Form ATS-R

What does the proposal do?

1) **THE PROPOSED DEFINITION OF "EXCHANGE"**: According to the Commission, the existing definition of "Exchange" does not capture many of the functions and methods used today for bringing buyers and sellers together and amending the definition would close this regulatory gap.

   - **"Non-Firm Trading Interest" versus "Orders"**: The current definition of "Exchange" revolves around the use of "orders" for bringing together buyers and sellers. "Non-firm trading interest" is not considered an "order," and therefore, does not fall under the existing definition of "Exchange" under the Act
     - Page 18 of the Final Proposal states, *"Further, at the time Exchange Act Rule 3b-16(a) was adopted, most ATSs operating met the criteria of the rule in that they offered the use of orders and algorithms that matched orders.[52] ATSs at that time allowed broker-dealers to place and execute orders on the system and the systems functioned as limit order books where orders are executed according to time, price, and size priority.[53] Accordingly, orders and established, non-discretionary methods undergirded Exchange Act Rule 3b-16 to reflect functions of exchange markets at that time. When discussing orders in the Regulation ATS Adopting Release, however, the Commission stated that systems that displayed bona fide, non-firm trading interest[54] or did not establish rules or operate a trading facility[55] would not fall within Rule 3b-16(a)"*

   - **Communication Protocol Systems (CPS)**: According to the Commission, the use of CPSs has grown, and generally, are viewed as mostly using "non-firm trading interest" to facilitate trades rather than what is defined under the Act as an "order"
     - Like "non-firm trading interest," CPSs do not fall under the current definition of an "Exchange" and are not required to comply with the same rules and regulations as registered exchanges or ATSs. By bringing them into the fold, CPSs that choose to operate as ATSs would need to comply with the existing Reg ATS provisions
     - The discussion around CPSs begins on page 18 of the proposal, and while the proposal does not provide a formal definition of what constitutes a CPS, the intention around the inclusion of CPSs is explained further on Page 25 Page 25: *"Given the changes in methods for bringing buyers and sellers together over the past couple of decades, the contrast between marketplace functions of exchanges that offer the use of orders and trading facilities and systems that offer the use of trading interest and protocols has become increasingly blurred. Both types of systems share the same business objectives and engage in similar market activities; however, one type of system is subject to the exchange regulatory framework while the other is not[66]*

       Today, Communication Protocol Systems perform similar marketplace functions as registered exchanges and ATSs and have become venues for investors to discover prices, find a counterparty, and agree upon the terms of a trade. Because Communication Protocol Systems do not fall within the definition of "exchange" and are thus not

required to register as national securities exchanges, they are not required to comply with the same federal securities laws and regulations applicable to registered exchanges[67] or ATSs[68]

- **Potential Implications for Decentralized Finance ("DeFi")**: The new definition of exchange could have implications for decentralized finance – e.g., cryptocurrency platforms
  - According to an article published by the National Law Review, "...if adopted as proposed, could "...sweep in currently unregulated blockchain-based cryptocurrency platforms and subject them to all of the regulatory requirements that flow from being an exchange. In short, the SEC is proposing a potentially transformative regulatory change that could create existential risks for DeFi platforms or, at the very least, fundamentally change the way they operate"

2) **EXPAND REGULATION ATS FOR ALTERNATIVE TRADING SYSTEMS THAT TRADE GOVERNMENT SECURITIES; EXTEND REGULATION SCI TO ATSs THAT TRADE GOVERNMENT SECURITIES**: Regulation has limited application to ATSs that trade government securities, so the proposal would no longer exempt from Reg ATS those ATS venues that limit securities activities or repurchase agreements or reverse repurchase agreements on government securities and is operated by a broker-dealer or is a bank.

The proposed amendments would also extend the requirements of Regulation SCI to Government Securities ATSs that during at least four of the preceding six calendar months had five percent or more of the average daily dollar volume traded in the U.S. for either U.S. Treasury Securities or Agency securities.

- **Proposed Definition of a Government Securities ATS** (Page 78)
  - The proposal would amend Rule 300 of Regulation ATS and define "Government Securities ATS" as an alternative trading system, as defined in Rule 300(a), that trades government securities, as defined in section 3(a)(42) of the Exchange Act (15 U.S.C. 78c(a)(42))[242]

    "The Commission is also re-proposing that a Government Securities ATS shall not trade securities other than government securities or repos[244] and that trading of securities other than government securities or repos would require the separate filing of a Form ATS or a Form ATS-N, depending on the types of securities traded[245]."

3) **AMENDMENTS TO FAIR ACCESS RULE FOR ALL ATS VENUES**: Proposed amendments to the Fair Access Rule would apply to all ATSs – i.e., NMS ATSs as well as newly defined Government Securities ATSs. The proposal would amend the Fair Access Rule, as well as the Capacity, Integrity, and Security Rule under Rule 301(b)(6), to specify the use of volume to calculate the relevant thresholds under the rule.

- **Aggregation of Volume Threshold for Affiliated ATSs**
  - The proposal would amend the Rule 301(b)(5)(ii) of the Fair Access Rule to aggregate the trading volume for a security or category of securities for ATSs that are operated by a common broker-dealer, or ATSs that are operated by affiliated broker-dealers
  - Aggregating trading volume among ATS marketplaces and Communication Protocol Systems would be subject to Regulation ATS under this proposal – either operated by a common broker-dealer or by affiliated broker-dealers

    Page 295 cites an example: *"As a result of this proposed change, if, for example, a broker-dealer operated two NMS Stock ATSs that each accounted for three percent of the average daily volume in an NMS stock during at least four of the preceding six calendar months, both NMS Stock ATSs would be subject to the Fair Access Rule for that security because their aggregated volume exceeds the five percent threshold of Rule 301(b)(5)(i)(A)[664]."*

Links to Additional Information

- SEC Press Release, Final Proposal, & Fact Sheet: https://www.sec.gov/news/press-release/2022-10
- Proposal Comment Letters: https://www.sec.gov/comments/s7-02-22/s70222.htm
- The National Law Review (Mar. 11, 2022): https://www.natlawreview.com/article/sec-proposes-to-redefine-exchange-new-definition-could-subject-blockchain-crypto

Proposal to Amend Investment Advisers Act of 1940 to Enhance Private Investor Protection

This proposal would increase transparency by requiring registered private fund advisers to provide investors with quarterly statements detailing certain information regarding fund fees, expenses, and performance.

- Require private fund advisers registered with the Commission to provide investors with quarterly statements detailing information about private fund performance, fees, and expenses
- Require registered private fund advisers to obtain an annual audit for each private fund and cause the private fund's auditor to notify the SEC upon certain events
- Require registered private fund advisers, in connection with an adviser-led secondary transaction, to distribute to investors a fairness opinion and a written summary of certain material business relationships between the adviser and the opinion provider
- Prohibit all private fund advisers, including those that are not registered, from engaging in certain activities and practices that are contrary to the public interest and the protection of investors; and
- Prohibit private fund advisers from providing certain types of preferential treatment that have a material negative effect on other investors, while also prohibiting all other types of preferential treatment unless disclosed to current and prospective investors.
- Additionally, the SEC is proposing to require all registered advisers, including those that do not advise private funds, to document the annual review of their compliance policies and procedures in writing

What does the proposal do?

1) THE QUARTERLY STATEMENT RULE

- The proposal would require **registered private fund advisers** to distribute a quarterly statement to private fund investors with a detailed accounting of all fees and expenses paid by the private fund during the reporting period. The statement would disclose information regarding compensation or other amounts paid by the private fund's portfolio investments to the adviser or any of its related persons
- The proposal would require advisers to provide information regarding the private fund's performance. **For liquid funds**, the quarterly statement would provide annual net total returns since inception, average annual net total returns over prescribed time periods, and quarterly net total returns for the current calendar year
- **For illiquid funds**, the statement would provide the gross and net internal rate of return and gross and net multiple of invested capital for the illiquid fund to capture performance from the fund's inception through the end of the current calendar quarter

2) THE PRIVATE FUND AUDIT RULE

- The proposal would require registered private fund advisers to cause the private funds they advise to undergo a financial statement audit **at least annually and upon liquidation**. The proposal would require audited financial statements be distributed to investors promptly after the completion of the audit

3) ADVISER-LED SECONDARIES RULE

- The proposal would require a registered private fund adviser to obtain a fairness opinion in connection with an adviser-led secondary transaction. In these transactions, advisers often offer existing fund investors the option to sell or exchange their interests in the private fund for interests in another vehicle advised by the adviser. An independent opinion provider would opine on the fairness of the price being offered to the private fund for any assets being sold as part of the transaction
- The proposal also would require the adviser to prepare and distribute to the private fund investors a summary of any material business relationships the independent opinion provider has or has had within the past two years with the adviser or any of its related persons. This requirement would provide a check against an adviser's conflicts of interest in structuring and leading a transaction from which it may stand to profit at the expense of private fund investors

4) **PROHIBITED ACTIVITES RULE**

- The proposal would prohibit all **private fund advisers** from engaging in certain activities and practices that are contrary to the public interest and the protection of investors. These practices are listed under section IX of the proposal (Page 339) and were also discussed in a recent article published by Institutional Investor
- **§ 275.211(h)(2)-1 Private Fund Adviser Prohibited Activities:** An investment adviser to a private fund may not, directly or indirectly, do the following with respect to the private fund, or any investor in that private fund. *(Defined terms shall have the meanings set forth in § 275.211(h)(1)-1)*
  - Charge a portfolio investment for monitoring, servicing, consulting, or other fees in respect of any services that the investment adviser does not, or does not reasonably expect to, provide to the portfolio investment
  - Charge the private fund for fees or expenses associated with an examination or investigation of the adviser or its related persons by any governmental or regulatory authority
  - Charge the private fund for any regulatory or compliance fees or expenses of the adviser or its related persons
  - Reduce the amount of any adviser clawback by actual, potential, or hypothetical taxes applicable to the adviser, its related persons, or their respective owners or interest holders
  - Seek reimbursement, indemnification, exculpation, or limitation of its liability by the private fund or its investors for a breach of fiduciary duty, willful misfeasance, bad faith, negligence, or recklessness in providing services to the private fund
  - Charge or allocate fees and expenses related to a portfolio investment (or potential portfolio investment) on a non-pro rata basis when multiple private funds and other clients advised by the adviser, or its related persons have invested (or propose to invest) in the same portfolio investment; and
  - Borrow money, securities, or other private fund assets, or receive a loan or an extension of credit, from a private fund client

5) **PREFERENTIAL TREATMENT RULE**

- The proposal would prohibit private fund advisers from providing preferential terms to certain investors regarding redemptions from the fund or information about portfolio holdings or exposures. It also prohibits private fund advisers from providing other preferential treatment unless disclosed to current and prospective investors. This proposal is designed to protect investors by prohibiting specific types of preferential treatment that have a material, negative effect on other investors

6) **BOOKS AND RECORDS RULE AMENDMENTS**

- The proposal includes amendments to the books and records rule under the Advisers Act that require advisers to retain records related to the proposed rules. The amendments would facilitate the SEC's ability to assess an adviser's compliance with the proposed rules

7) **COMPLIANCE RULE AMENDMENTS**

- The proposal includes amendments to the compliance rule under the Advisers Act that require all registered advisers, including those that do not advise private funds, to document their annual review in writing

Links to Additional Information

- SEC Press Release, Final Proposal, & Fact Sheet: https://www.sec.gov/news/press-release/2022-19
- Proposal Comment Letters: https://www.sec.gov/comments/s7-03-22/s70322.htm
- Institutional Investor (May 02, 2022): https://www.institutionalinvestor.com/article/b1xvz66l6zv8y4/The-SEC-s-Proposed-Rule-Could-Put-Investment-Managers-on-the-Hook-for-Losses-They-re-Not-Happy-About-it

Cybersecurity Risk Management for Investment Advisers, Registered Investment Companies, and Business Development Companies

This proposal introduces amendments to enhance cybersecurity preparedness and improve the resilience of investment advisers and investment companies against cybersecurity threats and attacks.

- Require advisers and funds to adopt and implement written policies and procedures reasonably designed to address cybersecurity risks
- Require advisers to report significant cybersecurity incidents to the Commission on proposed Form ADV-C
- Enhance adviser and fund disclosures related to cybersecurity risks and incidents; and
- Require advisers and funds to maintain, make, and retain certain cybersecurity-related books and records

What does the proposal do?

1) CYBERSECURITY RISK MANAGEMENT RULES

- The proposal includes **new rule 206(4)-9 under the Advisers Act and new rule 38a-2 under the Investment Company Act** (collectively, the **"proposed cybersecurity risk management rules"**). The proposed cybersecurity risk management rules would require advisers and funds to adopt and implement policies and procedures that are reasonably designed to address cybersecurity risks
- Advisers and funds would be required to address certain elements in their cybersecurity policies and procedures to help address operational and other risks that could harm advisory clients and fund investors or lead to the unauthorized access to or use of adviser or fund information, including the personal information of their clients or investors

2) REPORTING OF SIGNIFICANT CYBERSECURITY INCIDENTS

- A reporting requirement under **new rule 204-6** would require advisers to report significant cybersecurity incidents to the Commission, including on behalf of a fund or private fund client, by submitting a **new Form ADV-C**
- Specifically, any adviser registered or required to be registered with the Commission as an investment adviser would be required to submit proposed Form ADV-C promptly, **but in no event more than 48 hours**, after having a reasonable basis to conclude that a significant adviser cybersecurity incident or significant fund cybersecurity incident had occurred or is occurring[58]

3) DISCLOSURE OF CYBERSECURITY RISKS AND INCIDENTS

- The proposal would amend **Form ADV Part 2A** to require disclosure of cybersecurity risks and incidents to an adviser's clients and prospective clients. Currently, Form ADV Part 2A contains information about adviser's business practices, fees, risks, conflicts of interest, and disciplinary information
- Funds would be required to provide prospective and current investors with cybersecurity-related disclosures. **The proposed amendments would require a description of any significant fund cybersecurity incidents that have occurred in the last two fiscal years in funds' registration statements, tagged in a structured data language**
- The proposal amends **Form N-1A**, **Form N-2**, **Form N-3, Form N-4, Form N-6, Form N-8B-2, and Form S-6**

4) RECORDKEEPING

- Amendments to **Rule 204-2, the books and records rule under the Advisers Act**, to require advisers maintain certain records related to the proposed cybersecurity risk management rules and the occurrence of cybersecurity incidents
- **Proposed rule 38a-2 under the Investment Company Act** would require that a fund maintain copies of its cybersecurity policies and procedures and other related records specified under the proposed rule

Links to Additional Information

- SEC Press Release, Final Proposal, & Fact Sheet: https://www.sec.gov/news/press-release/2022-20
- Proposal Comment Letters: https://www.sec.gov/comments/s7-04-22/s70422.htm
- The National Law Review (Feb. 11, 2022): https://www.natlawreview.com/article/sec-issues-proposed-cyber-rule-including-48-hour-breach-reporting-requirement

Shortening the Securities Transaction Settlement Cycle

This proposal would:

- Shorten the standard settlement cycle for securities transactions from two business days after trade date (T+2) to one business day after trade date (T+1)
- Eliminate the separate T+4 settlement cycle for firm commitment offerings priced after 4:30 p.m.
- Improve the processing of institutional trades by proposing new requirements for broker-dealers and registered investment advisers intended to improve the rate of same-day affirmations; and
- Facilitate straight-through processing by proposing new requirements applicable to clearing agencies that are central matching service providers (CMSPs)
- **In the proposing release, the SEC proposed a compliance date of March 31, 2024**

What does the proposal do?

1) **PROPSAL FOR T+1 AND SHORTENING THE LENGTH OF THE STANDARD SETTLEMENT CYCLE**
   - **Amend Rule 15c6-1(a)** to prohibit a broker-dealer from effecting or entering into a contract for the purchase or sale of a security *(other than an exempted security, a government security, a municipal security, commercial paper, bankers' acceptances, or commercial bills)* that provides for payment of funds and delivery of securities later than the first business day after the date of the contract unless otherwise expressly agreed to by the parties at the time of the transaction[99]
   - The proposed amendment would change only the standard settlement date for securities transactions covered by the existing rule and would not impact the existing exclusions identified in the rule
   - **The proposal would retain the so-called "override provision"** and apply only to unusual cases to ensure that the settlement cycle set by Rule 15c6-1(a) is in fact the standard settlement cycle[100]
   - **Delete Rule 15c6-1(c)**, T+4 settlement cycle for firm commitment offerings for securities priced after 4:30 p.m. ET

2) **NEW REQUIREMENT FOR "SAME-DAY AFFIRMATION"**
   - **Proposed Rule 15c6-2 under the Exchange Act**: Allocation, confirmation and affirmation processes, or any combination thereof would require broker-dealers to have a written agreement with customers requiring these processes to be completed as soon as technologically practicable and no later than the end of the trade date
   - As proposed, the term "customer" is intended to cover the institutional investor and any and all agents acting on its behalf

3) PROPOSED AMENDMENTS TO RECORDKEEPING RULE FOR INVESTMENT ADVISERS

- **Proposed amendment to the investment adviser recordkeeping rule** to ensure registered investment advisers that are parties to contracts under proposed Rule 15c6-2 retain records of confirmations received, and keep records of the allocations and affirmations sent to a broker or dealer[175]
- For registered investment advisers that are parties to contracts under proposed Rule 15c6-2, **proposed amendment to Rule 204-2 under the Investment Advisers Act of 1940 (the "Advisers Act")** would require advisers maintain records of each confirmation received, and any allocation and each affirmation sent, with a date and time stamp for each allocation (if applicable) and affirmation that indicates when the allocation or affirmation was sent to the broker or dealer
- Under **Rule 204-2(a)(7)**, advisers would be required to keep originals of confirmations, and copies of allocations and affirmations, described in the proposed rule, but may maintain records electronically if they satisfy certain conditions[176]
- Proposed amendment to Rule 204-2 would require advisers to time and date stamp records of any allocation and each affirmation. Generally, advisers should time and date stamp records of each allocation (if applicable) and affirmation to the nearest minute

4) NEW REQUIREMENT FOR CMSPs TO FACILITATE STRAIGHT-THROUGH PROCESSING

- **Rule 17Ad-27** would require **central matching service providers (CMSPs)** to implement automatic processing of the entire trade process from execution through settlement without the need for manual intervention[184]
- **CMSPs facilitate straight-through processing** when its policies and procedures enable users to minimize or eliminate, to the extent that is technologically practicable, the need for manual input of trade details or manual intervention to resolve errors and exceptions that can prevent settlement of the trade

  "For example, a CMSP's policies and procedures generally should explain the criteria that the CMSP applies to determine when a "match" has been achieved, including any relevant tolerances that it or its users might apply to achieve a match, and the extent to which such criteria should be standardized or customized"
- **Proposed Rule 17Ad-27** also would require a CMSP to submit **every twelve months** to the Commission a report that describes the following:
  a) the CMSP's current policies and procedures for facilitating straight-through processing
  b) its progress in facilitating straight-through processing during the twelve-month period covered by the report; and
  c) the steps the CMSP intends to take to facilitate and promote straight-through processing during the twelve-month period that follows the period covered by the report
- Reports would be submitted via the Commission's Electronic Data Gathering, Analysis, and Retrieval system ("EDGAR")

5) IMPACT ON CERTAIN COMMISSION RULES, GUIDANCE, AND SRO RULES

- The proposal notes the proposed rules and amendments may affect compliance with other existing Commission rules and guidance that reference the settlement cycle or settlement processes in establishing requirements for market participants
- **A preliminary list of rules that could be impacted by shortening the settlement cycle are identified, however the Commission believes no changes are necessary**. Included are:
  1. Regulation SHO under the Exchange Act – Rules 204 & 200(g)
  2. Financial Responsibility Rules under the Exchange Act
  3. Rule 10b-10 under the Exchange Act
  4. Prospectus Delivery and "Access Versus Delivery"
  5. Changes to SRO Rules and Operations

6) PROPOSED COMPLIANCE DATE: MARCH 31, 2024

- The proposal states, "The proposed compliance date is based on the "T+1 Report" that a transition to T+1 is achievable in the first half of 2024. Additionally, planning for testing will begin in Q4 2022, industry-wide testing will begin in Q2 2023, and that industry-wide testing will need to occur for one full year before implementation of a T+1 standard settlement cycle"[228]

- According to the Commission, although the report estimates planning for testing will not begin until Q4 2022, and industry-wide testing will not begin until Q2 2023, it believes market participants can implement a T+1 standard settlement cycle by the earlier end of the T+1 Report's overall timetable
- In a comment letter, **SIFMA recommended** *"...at least two years from final rule publication to operationalize a T+1 settlement date*" to allow for the further development of existing discussions with respect to timing procedures and other market practices. SIFMA is also one of the members listed under the T+1 steering committee and working groups

T+1 Report: Illustration of Proposed Industry Migration Timeline & T+1 Settlement Trade Flow

The figure below assumes the necessary regulatory changes will be adopted in time to implement T+1 settlement Q1/Q2 2024

Figure 1: Proposed industry migration timeline

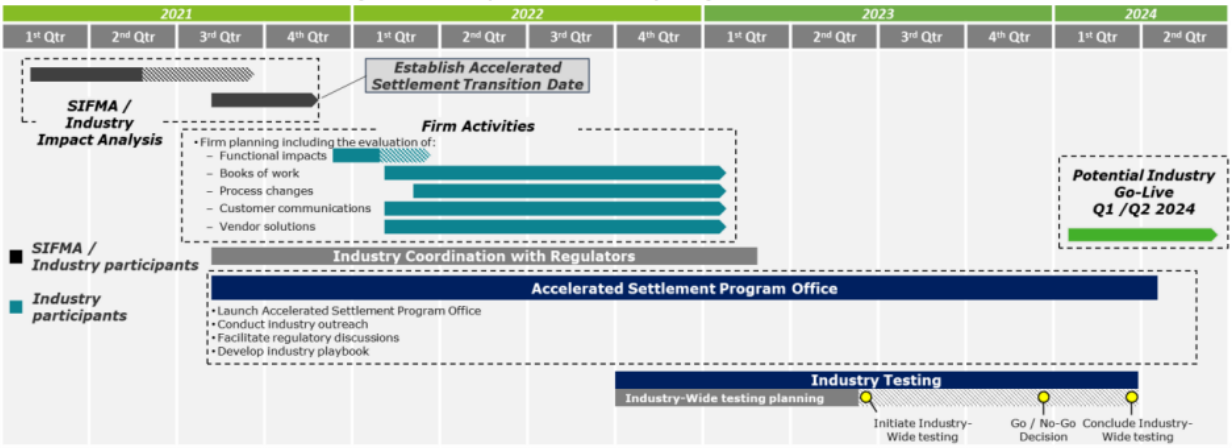
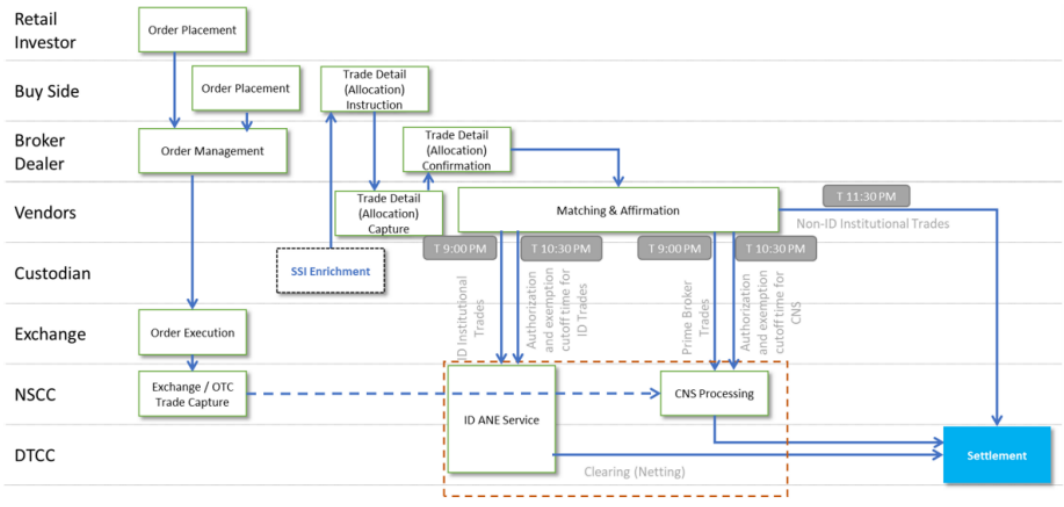


Figure 2: Illustrative T+1 settlement trade flow



Source: DTCC: Accelerating the U.S. Securities Settlement Cycle to T+1

Links to Additional Information

- SEC Press Release, Final Proposal, & Fact Sheet: https://www.sec.gov/news/press-release/2022-21
- Proposal Comment Letters: https://www.sec.gov/comments/s7-05-22/s70522.htm
- DTCC Accelerating to T+1: What You need To Know (Apr. 6, 2022): https://www.dtcc.com/dtcc-connection/articles/2022/april/06/accelerating-to-t1-what-you-need-to-know
- Industry information on the acceleration to T+1 settlement: ust1.org
- DTCC "T+1 Report" on settlement cycle, considerations, recommendations and next steps for moving to T+1 in the first half of 2024: https://www.dtcc.com/ust1/-/media/Files/PDFs/T2/Accelerating-the-US-Securities-Settlement-Cycle-to-T1-December-1-2021.pdf
- SIFMA Comment Letter dated April 13, 2022: https://www.sec.gov/comments/s7-05-22/s70522-20123609-279857.pdf

Modernization of Beneficial Ownership Reporting

This proposed amendments to Regulation 13D-G would:

- Accelerate the filing deadlines for Schedules 13D and 13G beneficial ownership reports
- Expand the application of Regulation 13D-G to certain derivative securities
- Clarify the circumstances under which two or more persons 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

What does the proposal do?

1) NEW SCHEDULE 13D AND 13G FILING DEADLINES

- **Schedule 13D**: The proposed amendments would shorten the initial filing deadline from **10 days to 5 days** following the acquisition of beneficial ownership of more than 5% or losing eligibility to file a Schedule 13G. The Proposal also requires Schedule 13D amendments to be filed **one business day** following a material change (versus the "prompt" requirement)
- **Certain Schedule 13G filers (i.e., qualified institutional investors and exempt investors)**: Proposal would shorten the initial filing deadline **from 45 days after year-end to 5 business days after the end of the month** in which their beneficial ownership exceeds 5% percent of the covered class
- **Other Schedule 13G filers (i.e., passive investors)**: Proposal would shorten the initial Schedule G filing deadline for passive investors **from 10 days to 5 days** after acquiring beneficial ownership of more than 5%
- **For all Schedule 13G filers**, the proposal would require an **amendment be filed 5 business days after the month in which a material change occurred versus 45 days after the year in which any change occurred**. The proposed amendments also would accelerate the amendment obligations for certain Schedule 13G filers upon exceeding 10 percent beneficial ownership or a 5 percent increase or decrease in beneficial ownership. Institutional investors and passive investors would file an amendment within 5 days and one day respectively
- **The proposal extends the deadline for filings from the current 5:30 p.m. ET to 10:00 p.m. ET**

2) REGULATION OF CERTAIN DERIVATIVE SECURITIES

- A holder of a cash-settled derivative security (other than security-based swaps which are under a separate rulemaking proposal from the SEC), will be deemed to be the beneficial owner of the shares referenced by the derivative security if the holder would be a Schedule 13D filer, even absent an express right to direct voting, acquisition or disposition of shares
- Proposed amendments would revise **Item 6 of Schedule 13D** to clarify a person is required to disclose interests in all derivative securities (including cash-settled derivative securities) that use the issuer's equity security as a reference security

3) CLARIFICATION OF GROUP FORMATION AND RELATED EXEMPTIONS

- **Under Regulation 13-DG and the Exchange Act**, the Proposal expands the definition of a **"group"** for reporting purposes from an agreement to act together to also include, depending on the particular facts and circumstances, concerted actions by two or more persons for the purpose of acquiring, holding or disposing of securities of an issuer
- Additionally, a group will exist where in advance of filing a Schedule 13D a filing person discloses to any other person that such filing will be made if the other person acquires securities subject to the Schedule 13D
- **Actions taken by two or more persons from forming a group are exempt** if "*...those actions do not have the purpose or effect of changing or influencing the control of an issuer and are not made in connection with or as a participant in any transaction having such purpose or effect"*

- Proposed changes of beneficial ownership and group formation rules apply when determining if a shareholder is subject to **Section 16** as a greater than 10% beneficial owner or part of a group that is over 10%

4) **STRUCTURED DATA REQUIREMENTS FOR SCHEDULES 13D AND 13G**

- The proposed amendments would require Schedules 13D and 13G be filed using a structured, machine-readable data language. This would require that all disclosures be filed with XML-based language for ease of investor access

Table Summarizing Proposed Changes as Depicted in the Final Proposal (Page 9)

Source: https://www.sec.gov/rules/proposed/2022/33-11030.pdf

Issue	Current Schedule 13D	Proposed New Schedule 13D	Current Schedule 13G	Proposed New Schedule 13G
Initial Filing Deadline	Within 10 days after acquiring beneficial ownership of more than 5% or losing eligibility to file on Schedule 13G. Rules 13d-1(a), (e), (f) and (g).	Within five days after acquiring beneficial ownership of more than 5% or losing eligibility to file on Schedule 13G. Rules 13d-1(a), (e), (f) and (g).	QIIs & Exempt Investors: 45 days after calendar year-end in which beneficial ownership exceeds 5%. Rules 13d-1(b) and (d). Passive Investors: Within 10 days after acquiring beneficial ownership of more than 5%. Rule 13d-1(c).	QIIs & Exempt Investors: Five business days after month-end in which beneficial ownership exceeds 5%. Rules 13d-1(b) and (d). Passive Investors: Within five days after acquiring beneficial ownership of more than 5%. Rule 13d-1(c).
Amendment Triggering Event	Material change in the facts set forth in the previous Schedule 13D. Rule 13d-2(a).	No amendment proposed – material change in the facts set forth in the previous Schedule 13D). Rule 13d-2(a).	All Schedule 13G Filers: Any change in the information previously reported on Schedule 13G. Rule 13d-2(b). QIIs & Passive Investors: Upon exceeding 10% beneficial ownership or a 5% increase or decrease in beneficial ownership. Rules 13d-2(c) and (d).	All Schedule 13G Filers: Material change in the information previously reported on Schedule 13G. Rule 13d-2(b). QIIs & Passive Investors: No amendment proposed – upon exceeding 10% beneficial ownership or a 5% increase or decrease in beneficial ownership. Rules 13d-2(c) and (d).
Amendment Filing Deadline	Promptly after the triggering event. Rule 13d-2(a).	Within one business day after the triggering event. Rule 13d-2(a).	All Schedule 13G Filers: 45 days after calendar year-end in which any change occurred. Rule 13d-2(b). QIIs: 10 days after month-end in which beneficial ownership exceeded 10% or there was, as of the month-end, a 5% increase or decrease in beneficial ownership. Rule 13d-2(c). Passive Investors: Promptly after exceeding 10% beneficial ownership or a 5% increase or decrease in beneficial ownership. Rule 13d-2(d).	All Schedule 13G Filers: Five business days after month-end in which a material change occurred. Rule 13d-2(b). QIIs: Five days after exceeding 10% beneficial ownership or a 5% increase or decrease in beneficial ownership. Rule 13d-2(c). Passive Investors: One business day after exceeding 10% beneficial ownership or a 5% increase or decrease in beneficial ownership. Rule 13d-2(d).
Filing "Cut-Off" Time	5:30 p.m. eastern time. Rule 13(a)(2) of Regulation S-T.	10 p.m. eastern time. Rule 13(a)(4) of Regulation S-T.	All Schedule 13G Filers: 5:30 p.m. eastern time. Rule 13(a)(2) of Regulation S-T.	All Schedule 13G Filers: 10 p.m. eastern time. Rule 13(a)(4) of Regulation S-T.

Links to Additional Information

- SEC Press Release, Final Proposal, & Fact Sheet: https://www.sec.gov/news/press-release/2022-22
- Proposal Comment Letters: https://www.sec.gov/comments/s7-06-22/s70622.htm
- Harvard Law School Forum on Corporate Governance (Mar. 6, 2022, Mar. 10, 2022): https://corpgov.law.harvard.edu/2022/03/06/sec-proposes-amendments-to-schedules-13d-and-13g/

The Commission's Whistleblower Program Rules

Section 21F of the Exchange Act authorizes the SEC to make monetary awards to eligible individuals who voluntarily provide original information that leads to successful SEC enforcement actions resulting in monetary sanctions exceeding $1 million and certain successful related actions.

The SEC is proposing two amendments to the rules governing its whistleblower program:

- Proposed amendment addressing instances when a whistleblower from the SEC's program receives an award from another, non-SEC, whistleblower program
- A second amendment affirming the SEC's authority to consider the dollar amount of a potential award for the limited purpose of increasing an award, but not to lower an award

What does the proposal do?

1) **RELATED ACTION CLAIMS COVERED BY ANOTHER WHISTLEBLOWER PROGRAM**

   - Under Exchange Act Section 21F(b) and Rule 21F-11, a whistleblower who obtains an award based on a Commission covered action also may be eligible for an award based on monetary sanctions that are collected in an action brought by other statutorily-identified authorities
   - The proposal would allow the Commission to make an award for a related action that might otherwise be covered by an alternative whistleblower program even where the alternative whistleblower program has the more direct or relevant connection to the related action in certain circumstances
   - The rule change is *"...designed to ensure that a whistleblower is not disadvantaged by another whistleblower program that would not give them as high an award as the SEC would offer"*
   - The proposed rule offers the following approaches:
     - **Comparability**
     - **Whistleblower Choice**
     - **Offset Approach**
     - **Topping Off Approach**

2) **DISCRETION TO CONSIDER THE DOLLAR AMOUNT OF THE AWARD**

   - The proposal affirms the Commission's authority to consider the dollar amount of a potential award for the limited purpose of increasing the award amount, but would eliminate the Commission's authority to consider the dollar amount of a potential award for the purpose of decreasing an award

Links to Additional Information

- SEC Press Release, Final Proposal, & Fact Sheet: https://www.sec.gov/news/press-release/2022-23
- Proposal Comment Letters: https://www.sec.gov/comments/s7-07-22/s70722.htm

Short Position and Short Activity Reporting by Institutional Investment Managers & Text of the Proposed Amendments to the NMS Plan Governing the Consolidated Audit Trail for Short Sale-Related Data Collection

- This proposal would:
  - ❖ Establish new Rule 13f-2 and amendments to Regulation SHO and CAT to increase market transparency regarding short selling
  - ❖ Proposed Rule 13f-2 and Form SHO would require institutional money managers file on the Commission's EDGAR system, on a monthly basis, certain short sale related data, some of which would be aggregated and made public
  - ❖ Certain data, including the identities of such managers and individual short positions, would remain confidential
  - ❖ To supplement the short sale data available to regulators, the Commission proposed a new provision of Regulation SHO under the Exchange Act — Proposed Rule 205 — as well as amendments to the consolidated audit trail plan (CAT). These amendments would require broker-dealers to collect and submit additional data on purchases to cover short sales as well as assertion of Regulation SHO's bona fide market making exceptions

What does the proposal do?

The following was directly sourced from the Harvard Law School forum on Corporate Governance. The entry was posted by Kevin J. Campion, Sidley Austin LLP and dated Saturday, April 2, 2022.

Link to full article: https://corpgov.law.harvard.edu/2022/04/02/the-secs-proposed-new-short-disclosure-sale-requirements/

1) **SUMMARY OF PROPOSED RULE 13F-2 AND PROPOSED FORM SHO**

- **Purpose**
  - **Proposed Rule 13f-2 and Proposed Form SHO** would improve the utility of information regularly available to the Commission, and made available as appropriate to self-regulatory organizations ("SROs"), that could be used to examine market behavior and recreate significant market events
  - It would also increase information available to market participants and could assist in their understanding of the level of negative sentiment and the actions of short sellers collectively
  - While the primary focus of Proposed Rule 13f-2 and Proposed Form SHO is transparency, the Commission's regular access to the data reported on Proposed Form SHO would also bolster its oversight of short selling

    Page 11: The Commission believes that publication of aggregated gross short position data of certain Managers, and certain related activity data would provide valuable transparency to market participants and regulators[24]

    The Commission believes that the data resulting from **Proposed Rule 13f-2** would help to provide valuable context to overall short position data currently available by distinguishing directional short selling of Managers from short sale activity effected pursuant to hedging as well as that of market makers and liquidity providers[25]

    The Commission believes that the data would provide regulators with a more complete picture of significant market events by shedding additional light on the potential role of short selling activity[26]

- **Securities Covered**: The **reporting requirements contained in proposed Rule 13f-2 and Form SHO** would apply to equity securities over which an Institutional Investment Manager and all accounts over which the Institutional Investment Manager (or any person under the Institutional Investment Manager's control) has investment discretion where the following thresholds are met:
  - Each equity security of an issuer registered pursuant to Section 12 of the Exchange Act or for which the issuer is required to file reports pursuant to Section 15(d) of the Exchange Act (Reporting Equity Securities) with either:
    - i. **a gross short position in the equity security with a U.S. dollar value of $10 million or more at the close of regular trading hours on any settlement date during the calendar month or**

ii. **a monthly average gross short position as a percentage of the issuer's total shares outstanding of 2.5% or more**

- Each equity security of an issuer that is not registered pursuant to Section 12 of the Exchange Act or for which the issuer is not required to file reports pursuant to Section 15(d) of the Exchange Act (Nonreporting Equity Securities) that has a gross short position with a U.S. dollar value of $500,000 or more at the close of regular trading on any settlement date during the calendar month

- **Gross Short Position Definition**: The reporting thresholds are based on an Institutional Investment Manager's gross short position in the equity security itself, and do not include short positions established through derivatives, such as options or swaps
  - However, the proposed Rule would require Institutional Investment Managers to report daily changes in their gross equity short position derived from acquiring or selling the equity in connection with derivative activity, such as exercising or getting assigned on an option
  - **"Gross short position" would mean the number of shares of the equity security that are held short, without inclusion of any offsetting long positions or economic long positions, including shares of the equity security or derivatives of such equity security**
- **Parties Covered and Responsible to Report**: The proposed reporting requirements would apply to Institutional Investment Managers, as defined for purposes of 13F reporting under the Exchange Act, that exercise investment discretion with respect to short positions meeting the above-described thresholds for Reporting Equity Securities and Nonreporting Equity Securities
  - While 13F reporting is limited to Institutional Investment Managers that generally exceed a threshold of exercising investment discretion in equity securities of $100 million, that would not be the case for Rule 13f-2 and Form SHO. Institutional Investment Managers that are not required to file Form 13F would still need to file Form SHO if they exceeded the above-described thresholds for Reporting Equity Securities and Nonreporting Equity Securities
- **Filing Deadlines for Reporting & Other Notifications**: Institutional Investment Managers that meet the thresholds would need to **file on Form SHO within 14 calendar days after the end of each calendar month**

  Amendments would be required for any errors and must restate Form SHO in its **entirety**
  - If the data being reported in the amendment affects the data reported on Form SHO reports filed in at least three of the immediately preceding Form SHO reporting periods, the Institutional Investment Manager would also within two business days after filing the amendment be required to notify the SEC staff of the amendment and provide an explanation of the reason for the amendment
- **Information to Be Reported on Form SHO**: Institutional Investment Managers would be required to provide extensive information concerning the end-of-month gross short position (both the number of shares and U.S. dollar value) and whether the identified short position is fully hedged or partially hedged
  - Information would be required regarding the short positions daily activity affecting the Institutional Investment Manager's gross short position for each settlement date during the calendar month reporting period such as:
    i. the number of shares sold short (including the number of shares sold in a put exercise or call option assignment)
    ii. the number of shares purchased to cover an existing short position (including the number of shares purchased in a call exercise or put option assignment)
    iii. number of shares obtained through secondary offering transactions
    iv. other activity that creates or increases a short position (including but not limited to shares resulting from exchange-traded fund (ETF) creation and redemption)
    v. other activity that reduces or closes a short position (including but not limited to shares resulting from ETF creation and redemption)
- **Aggregate Public Reporting by SEC**: The SEC would make public aggregated information derived from data reported on Form SHO within one month after the end of the reporting calendar month. For example, data reported on

Form SHO for the month of January would be published no later than the last day of February. Aggregated information published would include:

- the issuer's name and other identifying information related to the issuer
- the equity security's title of class, CUSIP number, and Financial Instrument Global Identifier (if applicable)
- the aggregated gross short position across all reporting Institutional Investment Managers in the reported security at the close of the last settlement date of the calendar month of the reporting period as well as the corresponding dollar value of the reported gross short position
- the percentage of the reported aggregate gross short position reported as being fully hedged, partially hedged, or not hedged
- for each settlement date during the calendar month reporting period, the "net" activity in the reported security as aggregated across all reporting Institutional Investment Managers

2) SUMMARY OF PROPOSED REGULATION SHO AND CAT CHANGES

- **New "Buy to Cover" Order Marking Requirement**: Proposed Rule 205 of Reg SHO would require a broker-dealer to mark a purchase order as "buy to cover" if, at the time of order entry, the purchaser (either the broker-dealer or another person) has a gross short position in such security in the specific account for which the purchase is being made at such broker-dealer
- A broker-dealer would be required to mark a purchase order as "buy to cover" regardless of its size in relation to the size of the purchaser's gross short position in the account and regardless of whether the gross short position is offset by a long position held in the purchaser's account at the time of order entry

  For example, *if the purchaser has a gross short position of 100 shares in a security in an account at a broker-dealer, then purchases 50 shares of such security for the same account at the same broker-dealer, the broker-dealer would be required to mark the purchase "buy to cover."*

  If, instead, there was a purchase of 150 shares of such security for the same account at the same broker-dealer (i.e., a purchase for an amount in excess of the total gross short position), then the SEC states that the broker-dealer would also be required to mark the purchase "buy to cover"
- **Reliance on Bona-Fide Market Making Exception**: The proposal would require CAT reporting firms that are reporting short sales to indicate whether such reporting firm is asserting use of the "bona-fide market maker exception" to the Reg SHO "locate" requirement
  - The Commission believes that requiring Industry Members to identify short sales for which they are claiming the bona fide market making exception would provide the Commission and other regulators an additional tool to determine whether such activity qualifies for the exception, or instead could be indicative of, for example, proprietary trading instead of bona fide market making[11]

3) BASELINE

- **Managers**
  - As of March 31, 2021, 7,550 Managers with investment discretion over approximately $39.79 trillion reported holdings on Form 13F in Section 13(f) securities[19]
  - The Commission also believes that registered investment advisers, particularly those managing hedge funds, are the primary Managers likely to be affected by the Proposed Rule
  - Though the Commission lacks data to quantify the number affected parties, the Commission estimates that the total number of Managers with reporting obligations will be between 346 and 1,000[194]
- **Short Selling**
  - Short sellers are involved in nearly 50% of trading volume, while only about 2% of shares outstanding are held short in the U.S. equity markets [199] This average volume of short selling tends to be much higher than the typical changes in short interest, [200] suggesting that a significant fraction of short selling volume is reversed very quickly. Such short selling may be more indicative of the fact that short selling is a key component of modern market making strategies and technical algorithmic trading [201]

4) THE EFFECT ON SHORT SELLING

According to the release, proposed Rule 13f-2 affects the value of short selling in four ways:

- Compliance costs, revealing short sellers' information, potentially revealing short sellers trading strategies, and increasing the threat of retaliation. Compliance costs associated with reporting large short positions are a direct increase in the cost of short selling.[268] As many Managers have underlying investors, these costs would likely be passed on to end consumers in the form of lower returns due to limiting the strategies that Managers could profitably employ
- Public release of the aggregated Proposed Form SHO data has the potential to reveal some of the information that short sellers may have acquired through fundamental research
- Third, the Proposed Form SHO data may provide information about the specific trading strategies of certain short sellers
- There is also evidence that when short sellers' positions become public, market participants strive to orchestrate short squeezes and are successful a significant fraction of the time[276]

5) BURDENS FOR MANAGERS UNDER PROPOSED RULE 13F-2 AND PROPOSED FORM SHO

- Page 96: The Commission estimates that, each month, **approximately 1,000 Managers would trigger a Reporting Threshold for at least one security**, and therefore be required to file a Proposed Form SHO[124]
- Accordingly, the Commission believes that the burden associated with preparing and filing Proposed Form SHO in EDGAR would be **~20 hours per filing**, consistent with that of former Form SHO
- The Commission further estimates that **Managers would collectively spend ~240,000 hours per year** to comply with the reporting requirements of Proposed Rule 13f-2[130]
- The Commission estimates that the hourly cost of internal expertise required for each filing would be $217.55, which includes a blended calculation of the estimated hourly rate for a compliance attorney, senior programmer, and in-house compliance clerk[131]
- Taken together the estimated burden hours and hourly rate for the filing of Proposed Form SHO result in an **estimated annual cost to the industry of $52,212,000** [132] The Commission, however, recognizes that advances in technology over time could result in Managers spending less time preparing and filing Proposed Form SHO than is estimated above[13]
- The Commission further **estimates that Managers would collectively spend up to ~24,000 hours and $6,480,000 per year** to file Proposed Form SHO directly in a structured XML-based data language[138]

6) BURDENS FOR BROKER DEALERS UNDER PROPOSED RULE 205

- Page 76: All broker-dealers whose accounts or whose customers' accounts at the broker-dealer could hold a short position are potentially subject to the requirements of Proposed Rule 205
- As of December 31, 2020, there were **3,551 broker-dealers registered with the Commission**[149]
- The Commission estimates that **of the 3,551 registered broker-dealers, 1,218 place orders that would require a "buy to cover"** order mark[150]

Links to Additional Information

- SEC Press Release, Final Proposal, & Fact Sheet: https://www.sec.gov/news/press-release/2022-32
- Proposal Comment Letters: https://www.sec.gov/comments/s7-08-22/s70822.htm
- Harvard Law School Forum on Corporate Governance (Apr. 2, 2022): https://corpgov.law.harvard.edu/2022/04/02/the-secs-proposed-new-short-disclosure-sale-requirements/
- The National Law Review (Apr.13, 2022): https://www.natlawreview.com/article/sec-proposes-short-sale-data-reporting-institutional-investment-managers

Cybersecurity Risk Management, Strategy, Governance, and Incident Disclosure

This proposal would:

- Require current reporting about material cybersecurity incidents on Form 8-K
- Require periodic disclosures such as:
  - A registrant's policies and procedures to identify and manage cybersecurity risks
  - Management's role in implementing cybersecurity policies and procedures
  - Board of directors' cybersecurity expertise, if any, and its oversight of cybersecurity risk; and
- Require the cybersecurity disclosures to be presented in Inline eXtensible Business Reporting Language (Inline XBRL)

What does the proposal do?

1) **REPORTING OF CYBERSECURITY INCIDENTS ON FORM 8K**

- **Proposed amendment to Form 8K by adding Item 1.05** would require registrants to disclose information about a cybersecurity incident within 4 business days after the registrant determines that it has experienced a material cybersecurity incident. According to the proposal, *"...information is material if there is a substantial likelihood that a reasonable shareholder would consider it important"*
- **The proposal defines the term "cybersecurity incident"** as *"...an unauthorized occurrence on or conducted through a registrant's information systems that jeopardizes the confidentiality, integrity, or availability of a registrant's information systems or any information residing therein. We also propose to define the term "information systems" as "information resources, owned or used by the registrant, including physical or virtual infrastructure controlled by such information resources, or components thereof, organized for the collection, processing, maintenance, use, sharing, dissemination, or disposition of a registrant's information to maintain or support the registrant's operations." The definitions of "cybersecurity incident" and "information systems" as proposed in Item 106 of Regulation S-K would also apply to such terms as used in proposed Item 1.05 of Form 8-K"*
- **Item 1.05 of Form 8K** would require disclosure of the following:
  - When the incident was discovered and whether it is ongoing
  - A brief description of the nature and scope of the incident
  - Whether any data was stolen, altered, accessed, or used for any other unauthorized purpose
  - The effect of the incident on the registrant's operations; and
  - Whether the registrant has remediated or is currently remediating the incident

  The proposed trigger for an Item 1.05 Form 8-K is the date on which a registrant determines that a cybersecurity incident it has experienced is material, rather than the date of discovery of the incident, so as to focus the Form 8-K disclosure on incidents that are material to investors
- Some **examples of cybersecurity incidents that may require disclosure** under proposed item 1.05 of Form 8K are listed on page 24 of the proposal (Link here: https://www.sec.gov/rules/proposed/2022/33-11038.pdf)

2) **DISCLOSURE ABOUT CYBERSECURITY INCIDENTS ON PERIODIC REPORTS**

- **Amend Forms 10-Q and 10-K** to require registrants to provide updated disclosure relating to previously disclosed cybersecurity incidents, as specified in **proposed Item 106(d) of Regulation S-K**
- Also proposed are amendments to these forms to require disclosure when a series of previously undisclosed individually immaterial cybersecurity incidents has become material in the aggregate.[38] Thus, registrants will need to analyze related cybersecurity incidents for materiality, both individually and in the aggregate

- **Examples**: "Proposed Item 106(d)(1) provides the following non-exclusive examples of the type of disclosure that should be provided, if applicable
  - Any material impact of the incident on the registrant's operations and financial condition
  - Any potential material future impacts on the registrant's operations and financial condition
  - Whether the registrant has remediated or is currently remediating the incident; and
  - Any changes in the registrant's policies and procedures as a result of the cybersecurity incident, and how the incident may have informed such changes

3) **DISCLOSURE OF A REGISTRANT'S RISK MANAGEMENT, STRATEGY AND GOVERNANCE REGARDING CYBERSECURITY RISKS**

- Amend Form 10-K to require disclosure specified in proposed **Item 106** regarding:
  - **Item 106(b) of Regulation S-K** would require disclosure of a registrant's policies and procedures, if it has any, to identify and manage cybersecurity risks and threats, including: operational risk; intellectual property theft; fraud; extortion; harm to employees or customers; violation of privacy laws and other litigation and legal risk; and reputational risk[39] (Page 38)
  - **Item 106(c)(1) of Regulation S-K**: A registrant's cybersecurity governance, including the board of directors' oversight role regarding cybersecurity risks;[40] and
  - **Item 106(c)(2) of Regulation S-K**: Management's role, and relevant expertise, in assessing and managing cybersecurity related risks and implementing related policies, procedures, and strategies[41]

4) **DISCLOSURE REGARDING THE BOARD OF DIRECTORS' CYBERSECURITY EXPERTISE**

- Proposed amendment to **Item 407 of Regulation S-K by adding paragraph (j)** to require disclosure about the cybersecurity expertise of members of the board of directors of the registrant, if any. If any member of the board has cybersecurity expertise, the registrant would have to disclose the name(s) of any such director(s), and provide such detail as necessary to fully describe the nature of the expertise[84]
- **Item 407(j) disclosure** would be required in a registrant's proxy or information statement when action is to be taken with respect to the election of directors, and in its Form 10-K
- Proposed **Item 407(j)(2)** would state that a person who is determined to have expertise in cybersecurity will not be deemed an expert for any purpose, including, without limitation, for purposes of Section 11 of the Securities Act,[85] as a result of being designated or identified as a director with expertise in cybersecurity[86]

5) **PERIODIC DISCLOSURE BY FOREIGN PRIVATE ISSUERS (FPI)**

- Amend **Form 20-F to add Item 16J** that would **require an FPI to include in its annual report on Form 20-F the same type of disclosure** proposed in Items 106 and 407(j) of Regulation S-K and that would be required in periodic reports filed by domestic registrants
- Where an FPI has previously reported an incident on **Form 6-K**, the proposed amendments would require an update regarding such incidents

6) **STRUCTURED DATA REQUIREMENTS**

- Disclosures to be provided in **Inline XBRL** in accordance with Rule 405 of Reg S-T and the EDGAR Filer Manual[92]

Links to Additional Information

- SEC Press Release, Final Proposal, & Fact Sheet: https://www.sec.gov/news/press-release/2022-39
- Proposal Comment Letters: https://www.sec.gov/comments/s7-09-22/s70922.htm
- The National Law Review (Mar. 11, 2022): https://www.natlawreview.com/article/sec-proposes-cybersecurity-rules-public-companies
- Harvard Law School Forum on Corporate Governance (Mar. 7, 2022): https://corpgov.law.harvard.edu/2022/03/07/f%E2%80%8Bour-takeaways-from-the-secs-proposed-cybersecurity-rules/

Enhancement and Standardization of Climate-Related Disclosures for Investors

This proposal would require a domestic or foreign registrant to include certain climate-related information in its registration statements and periodic reports, such as on Form 10-K, including:

- Climate-related risks and their actual or likely material impacts on the registrant's business, strategy, and outlook
- The registrant's governance of climate-related risks and relevant risk management processes
- The registrant's greenhouse gas ("GHG") emissions, which, for accelerated and large accelerated filers and with respect to certain emissions, would be subject to assurance
- Certain climate-related financial statement metrics and related disclosures in a note to its audited financial statements; and
- Information about climate-related targets and goals, and transition plan, if any

What does the proposal do?

1) PROPOSED AMENDMENTS TO REGULATION S-K AND REGULATION S-X

- **New subpart to Regulation S-K**, would require a registrant to disclose certain climate-related information, including information about its climate-related risks that are reasonably likely to have material impacts on its business or consolidated financial statements, and GHG emissions metrics that could help investors assess those risks[121].
- Inclusion of an attestation requirement for accelerated filers[122] and large accelerated filers[123] regarding certain proposed GHG emissions metrics disclosures[124] *(Accelerated filers and large accelerated filers are defined on page 41)*
- **New article to Regulation S-X** to require certain climate-related financial statement metrics and related disclosure to be included in a note to a registrant's audited financial statements.[125] The proposed financial statement metrics would consist of disaggregated climate-related impacts on existing financial statement line items. **Financial statement metrics would be subject to audit** by an independent registered public accounting firm, and come within the scope of the registrant's internal control over financial reporting ("ICFR")[126]

2) CONTENT OF PROPOSED DISCLOSURES

- The oversight and governance of climate-related risks by the registrant's board and management[127]
- How any climate-related risks identified by the registrant have had or are likely to have a material impact on its business and consolidated financial statements, which may manifest over the short-, medium-, or long-term[128]
- How any identified climate-related risks have affected or are likely to affect a registrant's strategy, business model, and outlook[129]
- The registrant's processes for identifying, assessing, and managing climate-related risks and whether any such processes are integrated into the registrant's overall risk management system or processes[130]
- The impact of climate-related events (severe weather events and other natural conditions as well as physical risks identified by the registrant) and transition activities (including transition risks identified by the registrant) on the line items of a registrant's consolidated financial statements and related expenditures,[131] and disclosure of financial estimates and assumptions impacted by such climate-related events and transition activities[132]
- Scopes 1 and 2 GHG emissions metrics, separately disclosed, expressed both by disaggregated constituent greenhouse gases and in the aggregate, and in absolute and intensity terms[133]
- Scope 3 GHG emissions and intensity, if material, or if the registrant has set a GHG emissions reduction target or goal that includes its Scope 3 emissions; and
- The registrant's climate-related targets or goals, and transition plan, if any[134]

3) PRESENTATION OF PROPOSED DISCLOSURES

- Proposed rules would require a registrant (both domestic and foreign private issuers[135]) to provide the climate-related disclosure in its registration statements and Exchange Act annual reports[136]
- Provide Regulation S-K mandated climate-related disclosures in a separate, appropriately captioned section of its registration statement or annual report, or alternatively to incorporate that information in the separate, appropriately captioned section by reference from another section, such as Risk Factors, Description of Business, or Management's Discussion and Analysis ("MD&A")[137]
- To provide the Regulation S-X mandated climate-related financial statement metrics and related disclosure in a note to the registrant's audited financial statements[138]
- To electronically tag both narrative and quantitative climate-related disclosures in Inline XBRL[139] and
- To file rather than furnish the climate-related disclosure[140]

4) ATTESTATION FOR SCOPE 1 AND SCOPE 2 EMISSIONS DISCLOSURE

- Require accelerated filer or a large accelerated filer to include, in the relevant filing, an attestation report covering, at a minimum, the disclosure of its Scope 1 and Scope 2 emissions and certain related disclosures about the service provider[141]
- Rules would provide minimum attestation report requirements, minimum standards for acceptable attestation frameworks, and would require an attestation service provider to meet certain minimum qualifications
- The proposed rules would not require an attestation service provider to be a registered public accounting firm

5) PHASE-IN PERIODS AND ACCOMMODATIONS FOR PROPOSED DISCLOSURES

- A phase-in period for all registrants, with the compliance date dependent on the registrant's filer status, and an additional phase-in period for Scope 3 emissions disclosure
- Phase-in period for the assurance requirement and level of assurance required for accelerated and large accelerated filers
- A safe harbor for liability for Scope 3 emissions disclosure
- An exemption from the Scope 3 emissions disclosure requirement for smaller reporting companies ("SRC");[143] and
- Forward-looking statement safe harbors pursuant to the Private Securities Litigation Reform Act, to the extent that proposed disclosures would include forward-looking statements

For explanatory purposes, the following tables assume that the proposed rules will be adopted with an effective date in December 2022 and that the filer has a December 31st fiscal year-end:

Registrant Type	Disclosure Compliance Date	
	All proposed disclosures, including GHG emissions metrics: Scope 1, Scope 2, and associated intensity metric, but excluding Scope 3	GHG emissions metrics: Scope 3 and associated intensity metric
Large Accelerated Filer	Fiscal year 2023 (filed in 2024)	Fiscal year 2024 (filed in 2025)
Accelerated Filer and Non-Accelerated Filer	Fiscal year 2024 (filed in 2025)	Fiscal year 2025 (filed in 2026)
SRC	Fiscal year 2025 (filed in 2026)	Exempted

Filer Type	Scopes 1 and 2 GHG Disclosure Compliance Date	Limited Assurance	Reasonable Assurance
Large Accelerated Filer	Fiscal year 2023 (filed in 2024)	Fiscal year 2024 (filed in 2025)	Fiscal year 2026 (filed in 2027)
Accelerated Filer	Fiscal year 2024 (filed in 2025)	Fiscal year 2025 (filed in 2026)	Fiscal year 2027 (filed in 2028)

Source: https://www.sec.gov/files/33-11042-fact-sheet.pdf

Links to Additional Information

- SEC Press Release, Final Proposal, & Fact Sheet: https://www.sec.gov/news/press-release/2022-46
- Proposal Comment Letters: https://www.sec.gov/comments/s7-10-22/s71022.htm
- Harvard Law School Forum on Corporate Governance (Apr. 8, 2022): https://corpgov.law.harvard.edu/2022/04/08/sec-proposes-landmark-standardized-disclosure-rules-on-climate-related-risks/
- The National Law Review (April 1, 2022): https://www.natlawreview.com/article/brief-summary-sec-s-proposed-climate-related-rules

Removal of References to Credit Ratings from Regulation M

This proposal would:

- Remove references to credit ratings currently included in Regulation M
- The measure of credit-worthiness of nonconvertible debt securities, nonconvertible preferred securities, and asset-backed securities included in the exception to Rule 101 of Regulation M would be replaced with new standards
- The exception to Rule 102 of Regulation M would be eliminated

Regulation M is a set of rules designed to preserve the pricing integrity of the securities trading markets by prohibiting issuers, selling security holders, distribution participants, and any of their affiliated purchasers from engaging in activities that could artificially influence the market for an offered security

What does the proposal do?

1) **PROPOSED AMENDMENTS TO RULES 101 & 102 TO REMOVE REFERENCES TO CREDIT RATINGS**

The Commission proposed to remove the requirement that nonconvertible debt securities, nonconvertible preferred securities, and asset-backed securities be rated investment grade by at least one nationally recognized statistical rating organization

- In place of that requirement, **under Rule 101, the Commission proposed to except**
  - Nonconvertible debt securities and nonconvertible preferred securities of issuers having a probability of default of less than 0.055%, as measured over certain period of time and as determined and documented using a "structural credit risk model," as defined in the rule, and
  - Asset-backed securities that are offered pursuant to an effective shelf registration statement filed on the Commission's Form SF-3
- **Proposal to eliminate from Rule 102** the existing exception for investment grade nonconvertible debt securities, nonconvertible preferred securities, and asset-backed securities

2) **RECORDKEEPING REQUIREMENT**

- A proposed **new recordkeeping requirement** requiring broker-dealers who are distribution participants or affiliated purchasers to keep certain records pursuant to Rule 17a-4 under the Exchange Act, the broker-dealer record retention rule
- Proposed new paragraph **(b)(17) of Rule 17a-4** would require broker-dealers who rely on the proposed exception in Rule 101 for certain nonconvertible debt securities and nonconvertible preferred securities to retain the written probability of default determination supporting their reliance on the exception
- **Rule 17a4(b)(17)** would require broker-dealers relying on Rule 101's exception for certain nonconvertible debt securities and nonconvertible preferred securities to preserve, for a period of not less than three years, the first two years in an easily accessible place, the written probability of default determination

Links to Additional Information

- SEC Press Release, Final Proposal, & Fact Sheet: https://www.sec.gov/news/press-release/2022-47
- Proposal Comment Letters: https://www.sec.gov/comments/s7-11-22/s71122.htm
- Mondaq (Apr. 7, 2022): https://www.mondaq.com/unitedstates/dodd-frank-consumer-protection-act/1180816/sec-proposes-to-remove-credit-ratings-references-from-regulation-m

Proposal to Include Certain Significant Market Participants as "Dealers" or "Government Securities Dealers"

This proposal would:

- Require market participants, such as proprietary (or principal) trading firms, that assume certain dealer-like roles and/or engage in certain levels of buying and selling government securities to register with the SEC, become a member of a self-regulatory organization ("SRO"), and comply with federal securities laws and regulatory obligations
- Rules 3a5-4 and 3a44-2 under the Exchange Act would set forth identical ***qualitative standards*** designed to identify market participants who assume certain dealer-like roles, in particular those who as act as liquidity providers in the markets
- Rule 3a44-2 would set forth a ***quantitative standard*** under which a person engaging in certain specified levels of activity would be deemed to be buying and selling government securities "as a part of a regular business," regardless of whether it meets any of the proposed rule's qualitative standards

What does the proposal do?

1) THE CURRENT DEFINITION OF "DEALER" & "GOVERNMENT SECURITIES DEALER"

- **"Dealer"**: Section 3(a)(5) of the Exchange Act defines the term "dealer" to mean "any person engaged in the business of buying and selling securities . . . for such person's own account through a broker or otherwise," but excludes "a person that buys or sells securities . . . for such person's own account, either individually or in a fiduciary capacity, but **not as a part of a regular business**"
- **"Government Securities Dealer"**: Similarly, Section 3(a)(44) of the Exchange Act, provides, in relevant part, that the term "government securities dealer" means "any person engaged in the business of buying and selling government securities for his own account, through a broker or otherwise," but "does not include any person insofar as he buys or sells such securities for his own account, either individually or in some fiduciary capacity, but **not as part of a regular business**"
- The purpose of the "trader" exception is to "exclude from the definition of 'dealer' members of the public who buy and sell securities for their own account as ordinary traders"[56]

2) PROPOSED RULES TO DEFINE ACTIVITIES THAT WOULD CONSTITUTE "REGULAR BUSINESS"

- **Qualitative Standards Under 3a5-4 and 3a44-2** Proposed rules further define standards for determining when the activity of a person that is engaged in buying and selling securities for its own account is "as a part of a regular business." According to the Commission, *"...dealer activity includes "...not only "acting as market maker" but also "acting as a de facto market maker whereby market professionals or the public look to the firm for liquidity"*[125]
- The proposal defines **3 patterns of buying and selling** as having the effect of providing liquidity
  - i. Routinely making roughly comparable purchases and sales of the same or substantially similar securities in a day
  - ii. Routinely expressing trading interests that are at or near the best available prices on both sides of the market and that are communicated and represented in a way that makes them accessible to other market participants
  - iii. Earning revenue primarily from capturing bid-ask spreads, by buying at the bid and selling at the offer, or from capturing any incentives offered by trading venues to liquidity-supplying trading interests
- Proposed rules would capture dealer activity **wherever that activity occurs**, whether on a national securities exchange, an ATS, a Communication Protocol System, or another form of trading venue
- **Quantitative Standard Under Rule 3a44-2**: A bright-line test under which persons engaging in certain specified levels of activity in the U.S. Treasury market would be defined to be buying and selling securities "as a part of a regular business," regardless of whether they meet any of the qualitative standards

- Under Rule 3a44-2, a person engaging in buying and selling for its own account more than $25 billion of trading volume in U.S. Treasury Securities in each of four out of the last six calendar months would be deemed "a part of a regular business"
- The "dealer" definition would be subject to a qualitative test, while the "government securities dealer" definition would be subject to both a qualitative and a quantitative test

3) DEFINITION OF "OWN ACCOUNT"

- Under the proposed rules a **person's "own account"** would mean any account:
  - held in the name of that person; or
  - held in the name of a person over whom that person exercises control or with whom that person is under common control, but not including:
    1) an account in the name of a registered broker, dealer, or government securities dealer, or an investment company registered under the Inv. Company Act of 1940, as amended (the "Investment Company Act"); or
    2) with respect to an investment adviser registered under the Investment Advisers Act of 1940, as amended (the "Investment Advisers Act"), an account held in the name of a client of the adviser unless the adviser controls the client as a result of the adviser's right to vote or direct the vote of voting securities of the client, the adviser's right to sell or direct the sale of voting securities of the client, or the adviser's capital contributions to or rights to amounts upon dissolution of the client; or
    3) with respect to any person, an account in the name of another person that is under common control with that person solely because both persons are clients of an investment adviser registered under the Investment Advisers Act unless those accounts constitute a parallel account structure; or
  - held for the benefit of those persons identified above
- Proposed definition of **"parallel account structure"** in anticipation of persons avoiding registration as dealers or government securities dealers through the structuring of funds (See examples page 85)

4) PERSONS EXCLUDED FROM THE PROPOSED RULES

- **Rules 3a5-4 and 3a44-2 would not apply** to:
  - Persons who have or control total assets of less than $50 million, or
  - Investment companies registered under the Investment Company Act
- **Proposed rules would not exclude private funds** because unlike registered investment companies, private funds are not subject to the extensive regulatory framework of the Investment Company Act
- **Proposed rules would not apply a blanket exclusion for registered investment advisers**. A registered investment adviser trading for its "own account" as defined in the proposal could implicate dealer registration requirements[117]
- See page 33 of the proposal for the discussion regarding persons excluded from the proposed rules and page 85 for examples with respect to aggregating and "parallel account structures"

Links to Additional Information

- SEC Press Release, Final Proposal, & Fact Sheet: https://www.sec.gov/news/press-release/2022-54
- Proposal Comment Letters: https://www.sec.gov/comments/s7-12-22/s71222.htm
- National Law Review (May 6, 2022): https://www.natlawreview.com/article/sec-proposes-rules-to-regulate-certain-market-participants-dealers-or-government
- Hinckley Allen (Apr. 4, 2022): https://www.hinckleyallen.com/publications/sec-proposes-changes-to-broaden-the-definitions-of-dealer-and-government-securities-dealer/

Proposal to Enhance Disclosure and Investor Protection Relating to SPACs, Shell Companies, and Projections

This proposal would:

- ❖ Enhance disclosures and provide additional investor protections in SPAC initial public offerings and in business combination transactions between SPACs and private operating companies (de-SPAC transactions)
- ❖ Address the treatment under the Securities Act of 1933 of business combination transactions involving a reporting shell company and amend the financial statement requirements applicable to transactions involving shell companies
- ❖ Provide additional guidance on the use of projections in SEC filings to address concerns about their reliability; and
- ❖ Assist SPACs in assessing when they may be subject to regulation under the Investment Company Act of 1940

What does the proposal do?

1) **PROPOSED NEW SUBPART 1600 OF REGULATION S-K FOR SPACs**

- **Subpart 1600 to Regulation S-K** requires specialized disclosures for SPACs regarding the sponsor, potential conflicts of interest, dilution, and to require certain disclosures on the prospectus cover page and in the prospectus summary[46]
- The following table summarizes the proposed items in Subpart 1600 (Table sourced from page 23 of the proposing release). Further details are below.

Item	Summary Description	Principal Objective(s)	Applicable forms and schedules
Item 1601, ***Definitions***	Definitions for the terms "special purpose acquisition company," "de-SPAC transaction," "target company," and "SPAC sponsor."	Establish the scope of the issuers and transactions subject to the requirements of Subpart 1600.	Forms S-1, F-1, S-4, and F-4; Schedules 14A, 14C, and TO
Item 1602, ***Registered offerings by special purpose acquisition companies***	Require certain information on the prospectus cover page and in the prospectus summary of registration statements for offerings by SPACs other than de-SPAC transactions. Require enhanced dilution disclosure in these registration statements.	Enhance the clarity and readability of prospectuses in SPAC initial public offerings and the disclosures relating to dilution in these prospectuses.	Forms S-1 and F-1
Item 1603, ***SPAC sponsor; conflicts of interest***	Require certain disclosure regarding the sponsor and its affiliates and any promoters of SPACs and disclosure regarding conflicts of interest between the sponsor or its affiliates or promoters and unaffiliated security holders.	Provide investors with a more complete understanding of the role of sponsors and their conflicts of interest.	Forms S-1, F-1, S-4, and F-4; Schedules 14A, 14C and TO
Item 1604, ***De-SPAC transactions***	Require certain information on the prospectus cover page and in the prospectus summary of registration statements for de-SPAC transactions. Require enhanced dilution disclosure in these registration statements.	Enhance the clarity and readability of prospectuses in de-SPAC transactions and disclosures relating to dilution in these prospectuses.	Forms S-4 and F-4; Schedules 14A, 14C, and TO
Item 1605, ***Background of and reasons for the de-SPAC transaction; terms of the de-SPAC transaction; effects***	Require disclosure on the background, material terms and effects of a proposed de-SPAC transaction.	Provide investors with a more complete understanding of the background of and motivations behind a proposed de-SPAC transaction.	Forms S-4 and F-4; Schedules 14A, 14C, and TO
Item 1606, ***Fairness of the de-SPAC transaction and any related financing transaction***	Require disclosure on whether a SPAC reasonably believes that a de-SPAC transaction and any related financing transactions are fair or unfair to investors, as well as a discussion of the bases for this reasonable belief.	Provide investors with additional information regarding a proposed de-SPAC transaction and address concerns regarding potential conflicts of interest and misaligned incentives.	Forms S-4 and F-4; Schedules 14A, 14C, and TO
Item 1607, ***Reports, opinions, appraisals and negotiations***	Require disclosure on whether a SPAC or its sponsor has received a report, opinion or appraisal from an outside party regarding the fairness of a de-SPAC transaction or any related financing transaction.	Provide investors with additional information underlying a fairness determination by a SPAC.	Forms S-4 and F-4; Schedules 14A, 14C, and TO
Item 1608, ***Tender offer filing obligations in de-SPAC transactions****	Require additional disclosures in a Schedule TO filed in connection with a de-SPAC transaction.	Align the information provided in such a Schedule TO with the information provided in other filings in connection with a de-SPAC transaction.	Schedule TO
Item 1609, ***Financial projections in de-SPAC transactions*****	Require additional disclosures regarding financial projections disclosed in a disclosure document for a de-SPAC transaction.	Provide investors with additional information regarding the use of projections in connection with a de-SPAC transaction.	Forms S-4 and F-4; Schedules 14A, 14C, and TO
Item 1610, ***Structured data requirement*****	Require information disclosed pursuant to Subpart 1600 to be tagged in a structured, machine-readable data language.	Provide investors and other market participants with information that is more readily available and more easily accessible for aggregation, comparison, filtering, and other analysis	Forms S-1, F-1, S-4, and F-4; Schedules 14A, 14C, and TO

- **Item 1603(a) to require additional disclosure about the sponsor, its affiliates and any promoters[63] of the SPAC** in registration statements and schedules filed in connection with SPAC registered offerings and de-SPAC transactions, including disclosure on the following:
  - The experience, material roles, and responsibilities of these parties, as well as any agreement, arrangement or understanding (1) between the sponsor and the SPAC, its executive officers, directors or affiliates, in determining whether to proceed with a deSPAC transaction and (2) regarding the redemption of outstanding securities
  - Controlling persons of the sponsor and persons having direct and indirect material interests in the sponsor, as well as an organizational chart that shows the relationship between the SPAC, the sponsor, and the sponsor's affiliates
  - Tabular disclosure of the material terms of any lock-up agreements with the sponsor and its affiliates; and
  - The nature and amounts of all compensation that has or will be awarded to, earned by, or paid to the sponsor, its affiliates and any promoters for all services rendered in all capacities to the SPAC and its affiliates, as well as the nature and amounts of any reimbursements to be paid to the sponsor, its affiliates and any promoters upon the completion of a de-SPAC transaction[64]
- **Item 1603(b) would require disclosure of any actual or potential material conflict of interest** between (1) the sponsor or its affiliates or the SPAC's officers, directors, or promoters, and (2) unaffiliated security holders. This would include any conflict of interest in determining whether to proceed with a de-SPAC transaction and any conflict of interest arising from the manner in which a SPAC compensates the sponsor or the SPAC's executive officers and directors, or the manner in which the sponsor compensates its own executive officers and directors. **Item 1603(c) would require disclosure regarding the fiduciary duties** each officer and director of a SPAC owes to other companies
- **Items 1602(a)(4), 1602(c) and 1604(c)** would require additional **disclosure about the potential for dilution** in (1) registration statements filed by SPACs, including those for initial public offerings, and (2) de-SPAC transactions. Proposed Item 1602(c) would be applicable to all registered offerings by a SPAC other than a de-SPAC transaction, while proposed Item 1604(c) would be applicable to all de-SPAC transactions. **Item 1602(a)(4)** would require simplified tabular **dilution disclosure on the prospectus cover page** in registered offerings by a SPAC on Form S-1 or F-1 other than for de-SPAC transactions
- **Item 1602** would require that certain information be included on the **prospectus cover page and in the prospectus summary** using plain English principles[79]
  - **Prospectus Cover Page**: Item 1602(a) would require information on the prospectus cover page the time frame for the SPAC to consummate a de-SPAC transaction, redemptions, sponsor compensation, dilution (including simplified tabular disclosure), and conflicts of interest. For de-SPAC transactions, Item 1604(a) would require information on the prospectus cover page, such as fairness of the de-SPAC transaction, material financing transactions, sponsor compensation and dilution, and conflicts of interest
  - **Prospectus Summary**

    Item 1602(b) would require **SPACs include the following in the prospectus summary**:
    - The process by which a potential business combination candidate will be identified and evaluated
    - Whether shareholder approval is required for the de-SPAC transaction
    - The material terms of the trust or escrow account, including the amount of gross offering proceeds that will be placed in the trust
    - The material terms of the securities being offered, including redemption rights
    - Whether the securities being offered are the same class as those held by the sponsor and its affiliates
    - The length of the time period during which the SPAC intends to consummate a de-SPAC transaction, and its plans if it does not do so, including, whether and how the time period may be extended, the consequences to the sponsor of not completing an extension of this time period, and whether shareholders will have voting or redemption rights with respect to an extension of time to consummate a de-SPAC transaction
    - Any plans to seek additional financing and how such additional financing might impact shareholders
    - Tabular disclosure of sponsor compensation and the extent to which material dilution may result from such compensation; and
    - Material conflicts of interest

- **For registered de-SPAC transactions, Item 1604(b) would require in the prospectus summary**:
  - The background and material terms of the de-SPAC transaction
  - The fairness of the de-SPAC transaction
  - Material conflicts of interest
  - Tabular disclosure on sponsor compensation and dilution
  - Financing transactions in connection with de-SPAC transactions; and
  - Redemption rights

2) DISCLOSURE AND PROCEDURAL REQUIREMENTS IN DE-SPAC TRANSACTIONS

- **Background of and Reasons for the De-SPAC Transaction; Terms and Effects**: Item 1605 of Regulation S-K would require disclosure of the background, material terms, and effects of the de-SPAC transaction, including:
  - A summary of the background of the de-SPAC transaction, including, but not limited to, a description of any contacts, negotiations, or transactions that have occurred concerning the de-SPAC transaction[85]
  - A brief description of any related financing transaction, including any payments from the sponsor to investors in connection with the financing transaction
  - The reasons for engaging in the particular de-SPAC transaction and for the structure and timing of the de-SPAC transaction and any related financing transaction
  - An explanation of any material differences in the rights of security holders of the post-business combination company as a result of the de-SPAC transaction[86] and
  - Disclosure of accounting treatment and the federal income tax consequences of the de-SPAC, if material[87]
- **Fairness of the De-SPAC Transaction**: Items 1606(c), (d), and (e), which would require disclosure on whether:
  - The de-SPAC transaction or any related financing transaction is structured so that approval of at least a majority of unaffiliated security holders is required
  - A majority of directors who are not employees of the SPAC has retained an unaffiliated representative to act solely on behalf of unaffiliated security holders for purposes of negotiating the terms of the de-SPAC transaction or any related financing transaction and/or preparing a report concerning the fairness of the de-SPAC transaction or any related financing transaction; and
  - The de-SPAC transaction or any related financing transaction was approved by a majority of the directors of the SPAC who are not employees of the SPAC
- **Reports, Opinions, and Appraisals**: Item 1607(a) would require disclosure about whether or not the SPAC or its sponsor has received any report, opinion, or appraisal obtained from an outside party relating to the consideration or the fairness of the consideration to be offered to security holders or the fairness of the de-SPAC transaction or any related financing transaction to the SPAC, the sponsor or security holders who are not affiliates[98]
- **Proposed Item 1608 of Regulation S-K**: Proposed Item 1608 would require a SPAC that files a Schedule TO for any redemption of securities offered in connection with a de-SPAC transaction to include disclosures required by specified provisions of Forms S-4 and F-4, and Schedule 14A, as applicable

  SPAC shareholders who are not solicited for their votes to approve a de-SPAC transaction (in a solicitation subject to Regulation 14A) would receive the same information about the target private operating company that could be material to their redemption decisions[104]

3) ALIGNING DE-SPAC TRANSACTIONS WITH IPOs

- **Aligning Non-Financial Disclosures in De-SPAC Disclosure Documents**: For target companies in a de-SPAC transaction not subject to the reporting requirements of Section 13(a) or 15(d) of the Exchange Act, disclosure in Regulation S-K would be required. This would mandate information about the private operating company be provided to shareholders before they make voting, investment, or redemption decisions[126]
- **Minimum Dissemination Period**: Requirement that prospectuses and proxy and information statements filed in connection with de-SPAC transactions be distributed to shareholders at least 20 calendar days in advance of a shareholder meeting or the earliest date of action by consent[129]

- **Private Operating Company as Co-Registrant to Form S-4 and Form F-4**: Amended Forms S-4 and F-4 would require that the SPAC and the target company be treated as co-registrants when these registration statements are filed by the SPAC in connection with a de-SPAC transaction[141]
- **Re-determination of smaller reporting company status** following the consummation of a de-SPAC transaction
- **PSLRA Safe Harbor**: Amends the definition of "blank check company" for purposes of the PSLRA to encompass SPACs (and some other blank check companies) such that the safe harbor under PSLRA for forward-looking statements (including with respect to the use of projections) would not be available to SPACs or to target companies engaging in a de-SPAC
- **Underwriter Status and Liability in Securities Transactions**: Rule 140a would deem anyone who has acted as an underwriter of the securities of a SPAC IPO, and who takes steps to facilitate a de-SPAC (or any related financing, or who otherwise participates, directly or indirectly, in the de-SPAC), to be engaged in a distribution and to be an underwriter of the securities in the de-SPAC

"Clarifying the underwriter status of SPAC IPO underwriters in connection with de-SPAC transactions should motivate them to exercise the care necessary to help ensure the accuracy of the disclosures in these transactions by affirming that they are subject to Section 11 liability for registered deSPAC transactions"[201]

4) **BUSINESS COMBINATIONS INVOLVING SHELL COMPANIES**

- New Rule 145a under the Securities Act would deem any business combination of a reporting shell company[227] involving another entity that is not a shell company to involve a sale of securities to the reporting shell company's shareholders[228]
- Article 15 of Regulation S-X and related amendments would address inconsistencies in the reporting of financial information that can arise when applying existing requirements to business combination transactions involving shell companies compared to the financial statement requirements for a Securities Act registration statement

5) **ENHANCED PROJECTIONS DISCLOSURE**

- **Item 10(b)**, which currently refers to **projections regarding future performance of a "registrant,"** would state:
  - Any projected measures that are not based on historical financial results or operational history should be clearly distinguished from projected measures that are based on historical financial results or operational history
  - It generally would be misleading to present projections that are based on historical financial results or operational history without presenting such historical measure or operational history with equal or greater prominence; and
  - The presentation of projections that include a non-GAAP financial measure should include a clear definition or explanation of the measure, a description of the GAAP financial measure to which it is most closely related,286 and an explanation why the non-GAAP financial measure was used instead of a GAAP measure[287]
- **Item 1609** would require disclosures intended to assist investors in assessing the bases of projections used on de-SPAC transactions and determining to what extent they should rely on such projections

6) **PROPOSED SAFE HARBOR UNDER THE INVESTMENT COMPANY ACT**

- Proposed **Rule 3a-10** would provide a safe harbor such that a SPAC would not be an "investment company" if:
  i. the SPAC's only assets are cash items, government securities, and certain money market funds
  ii. the SPAC seeks to complete a de-SPAC, after which the surviving entity will be primarily engaged in the business of the target company; and
  iii. the SPAC enters into an agreement with the target company to engage in a de-SPAC within 18 months after its IPO, and completes the de-SPAC within 24 months of the offering

Links to Additional Information

- SEC Press Release, Final Proposal, & Fact Sheet: https://www.sec.gov/news/press-release/2022-56
- Proposal Comment Letters: https://www.sec.gov/comments/s7-13-22/s71322.htm
- Harvard Law School Forum on Corporate Governance (Apr. 22, 2022): https://corpgov.law.harvard.edu/2022/04/22/sec-rules-would-make-spac-process-more-burdensome-than-traditional-ipos/

Rules Relating to Security-Based Swap Execution and Registration and Regulation of Security-Based Swap Execution Facilities

This proposal would:

- Create a regime for the registration and regulation of security-based swap execution facilities (SBSEFs);
- Implement the "trade execution requirement" for security-based swaps (SBS) and address various issues relating to the requirement, including its cross-border application
- Address conflicts of interest at SBSEFs and national securities exchanges that trade SBS; and
- Promote consistency between the proposed rules governing SBSEFs and existing rules under the Exchange Act

What does the proposal do?

1) REGULATION SE

- Regulation SE would establish a new **framework for the registration and regulation of security-based swap execution facilities (SBSEFs)**. Registration would be submitted via new Form SBSEF
- The **definition of "security-based swap execution facility"** would not include an entity registered with the Commission as a clearing agency and limits its security-based swap matching functions to operation of a trading session that is designed to further the accuracy of end-of-day valuations
- Entities meeting the definition of "security-based swap execution facility" must:
  - Register with the Commission as an SBSEF on Form SBSEF or register as a national securities exchange; and
  - Foreign SBS trading venues may seek an exemption from the definition of "security-based swap execution facility" pursuant to proposed Rule 833(a)

2) REGISTERED SBSEF REQUIREMENTS

- Submit filings **w**ith the Commission for new rules, rule amendments, or products
- Submit information requested by the Commission, including compliance with Core Principles, notification of a transfer of **50% or more of the equity interest** in the SBSEF, and pending legal proceedings
- Establish, comply, and enforce rules regarding market access, trading and trade processing, the operation of the SBSEF, the financial integrity of SBS on its facility, the exercise of emergency authority, and conflicts of interest
- Monitor trading and market activity to prevent manipulation, price distortion, and delivery or settlement disruptions
- Make public timely information on price, trading volume, and other trading data on SBS transactions, as required by Regulation SBSR, and publish on its website a Daily Market Data Report
- Maintain records of all activities, including a complete audit trail, **for a period of five years**
- Have adequate financial, operational, and managerial resources to discharge its responsibilities
- Establish and maintain a program of automated systems and risk analysis to identify and minimize operational risk
- Establish and maintain emergency procedures, backup facilities, and a disaster recovery plan; and
- Designate a chief compliance officer (CCO) and establish regulatory and reporting obligations for the CCO

Links to Additional Information

- SEC Press Release, Final Proposal, & Fact Sheet: https://www.sec.gov/news/press-release/2022-59
- Proposal Comment Letters: https://www.sec.gov/comments/s7-14-22/s71422.htm
- National Law Review (May 6, 2022): https://www.natlawreview.com/article/sec-issues-rule-proposal-security-based-swap-execution-facilities

Investment Company Names – Amendments to the Fund "Names Rule"

This proposal would amend Rule 35d-1 under the Investment Company Act of 1940 by:

- ❖ Improving and expanding the current requirement for certain funds to adopt a policy to invest at least **80 percent** of their assets in accordance with the investment focus the fund's name suggests
- ❖ Providing new enhanced disclosure and reporting requirements; and
- ❖ Updating the rule's current notice requirements and establishing recordkeeping requirements

What does the proposal do?

1) **80% INVESTMENT POLICY REQUIREMENT**

- **Names Suggesting an Investment Focus**: The proposal broadens the scope of the name rule's current 80% investment policy requirement to apply to fund names that include terms suggesting that the fund focuses in investments that have, or whose issuers have, particular characteristics[31]
  - The proposed amendments provide as examples fund names with terms such as "growth" or "value," or terms indicating that the fund's investment decisions incorporate one or more ESG factors[32]
  - Under the proposed amendments, where a fund's name suggests an investment focus that has multiple elements, the fund's 80% investment policy must address each element
- **The proposed amendments would permit a fund to depart temporarily from the requirement** to invest at least 80% of the value of its assets in accordance with the investment focus or tax treatment its name suggests ("80% investment requirement") under specified circumstances. These **temporary departures would be permitted only**:
  - as a result of market fluctuations, or other circumstances where the temporary departure is not caused by the fund's purchase or sale of a security or the fund's entering into or exiting an investment
  - address unusually large cash inflows or unusually large redemptions
  - to take a position in cash and cash equivalents or government securities to avoid a loss in response to adverse market, economic, political, or other conditions; or
  - to reposition or liquidate a fund's assets in connection with a reorganization, to launch the fund, or when notice of a change in the fund's 80% investment policy has been provided to fund shareholders at least 60 days before the change pursuant to the rule[55]
- **Considerations Regarding Derivatives in Assessing Names Rule Compliance**: The proposed amendments would require that, in calculating its assets for purposes of names rule compliance, a fund must value each derivatives instrument using its notional amount, with certain adjustments, and reduce the value of its assets by excluding cash and cash equivalents up to the notional amounts of the derivatives instrument(s).[74] When a fund determines its compliance with its 80% investment policy, all derivatives instruments would be included in the denominator in the calculation, as well as any derivatives in the fund's 80% basket, i.e., the numerator in the calculation
- **Unlisted Closed-End Funds and BDCs**: A requirement that a fund's 80% investment policy must always be a fundamental investment policy if the fund is a registered closed-end investment company or BDC that does not have shares listed on a national securities exchange. **Unlisted closed-end funds and BDCs would not be permitted to change their 80% investment policies without shareholder approval**
- **Compliance**: **A fund's name may be materially deceptive or misleading under section 35(d) even if the fund adopts an 80% investment policy and otherwise complies with the rule's requirements**. If, for example, a fund complies with its 80% investment policy but makes a substantial investment that is antithetical to the fund's investment focus (e.g., a "fossil fuel-free" fund making a substantial investment in an issuer with fossil fuel reserves)

2) PROSPECTUS DISCLOSURE DEFINING TERMS USED IN FUND NAME

The proposal would amend funds' registration forms – specifically, **Form N-1A**, **Form N-2**, Form **N-8B-2**, and **Form S-6** – that would require each fund that is required to adopt and implement an 80% investment policy to include disclosure in its prospectus that defines the terms used in its name, including the specific criteria the fund uses to select the investments that the term describes, if any.

3) PLAIN ENGLISH/ESTABLISHED INDUSTRY USE REQUIREMENT

- The requirement that any terms used in the fund's name that suggest either an investment focus, or that such fund is a tax-exempt fund, must be **consistent with those terms' plain English meaning or established industry use**[116]
- The proposed plain English or established industry use requirement would address concerns that a fund sponsor may subvert an investor's reasonable expectations of a fund's investment focus by using terminology in the fund's name in a manner that is inconsistent with the plain English or established industry use
- **For example**, a fund that calls itself a "solar energy fund" would not be able to use disclosure to qualify the name in the prospectus by stating he fund's 80% basket includes investments in securities of any type of alternative energy company

4) MATERIALLY DECEPTIVE & MISLEADING USE OF ESG TERMINOLOGY IN CERTAIN FUND NAMES

- The proposed amendments address what is refer to in this release as **"integration funds,"** and would define the names of "integration funds" as materially deceptive and misleading if the name includes terms suggesting the fund's investment decisions incorporate one or more **ESG factors**
- As used in this release, **integration funds are funds that consider one or more ESG factors alongside other, non-ESG factors** in the fund's investment decisions but those ESG factors are generally no more significant than other factors in the investment selection process, such that ESG factors may not be determinative in deciding to include or exclude any particular investment in the portfolio[118]. *Under the Proposed Amendments, a fund cannot include ESG in its name if ESG factors are not the determinative consideration in investment decisions or if the fund makes substantial investments that are contrary to its ESG factors, even when those investments are within the other 20% basket under an 80% Policy*

5) MODERNIZING THE RULE'S NOTICE REQUIREMENT

- The proposed amendments would require that unless the 80% investment policy is a fundamental policy of the fund, **notice must be provided to fund shareholders** of any change in the fund's 80% investment policy[126]
- As an additional modification, the proposed amendments would require notices to describe not only a change in the fund's 80% investment policy, but also a change to the fund's name that accompanies the investment policy change
- The proposal retains **the notice alternative** to provide eligible funds flexibility to respond efficiently to market events or new regulatory requirements

6) N-PORT REPORTS

- Proposed **amendments to Form N-PORT** to require greater transparency on how fund investment selection methods match the investment focus that the fund's name suggests. These new reporting items would disclose:
  - i. the value of the fund's **80% basket**, as a percentage of the value of the fund's assets
  - ii. for each portfolio investment, whether it's included in the fund's 80% basket at the end of the period, and
  - iii. if applicable, the number of days that the value of the fund's 80% basket fell below 80% of the value of the fund's assets during the reporting period. These proposed N-PORT requirements would not be applicable to money market funds

7) RECORDKEEPING

- The proposed amendments require a fund that is required to adopt an 80% investment policy to **maintain written records documenting its compliance under the 80% investment policy provisions** of the rule. Specifically, the written records documenting the fund's compliance that these funds would be required to maintain would include:

  - A record of which investments are included in the fund's 80% basket (generally investments that are invested in accordance with the investment focus the fund's name suggests or, as applicable, consistent with the tax treatment suggested by a tax-exempt fund's name) and the basis for including each such investment in the 80% basket
  - The value of the fund's 80% basket, as a percentage of the value of the fund's assets
  - The reasons for any departures from the 80% investment policy
  - The dates of any departures from the 80% investment policy; and
  - Any notice sent to the fund's shareholders pursuant to the rule[152]

- Records must be **maintained for at least six years** following the creation of each required record (or, in the case of notices, following the date the notice was sent), the first two years in an easily accessible place[153]
- Proposal would require **funds that do not adopt an 80% investment policy** under the rule to maintain a written record of the fund's analysis that an 80% investment policy is not required[157]

8) **UNIT INVESTMENT TRUSTS**

- Proposed rule amendments would include certain exceptions for unit investment trusts ("UITs") that have made their initial deposit of securities prior to the effective date of any final rule amendments the Commission adopts

Links to Additional Information

- SEC Press Release, Final Proposal, & Fact Sheet: https://www.sec.gov/news/press-release/2022-91
- Proposal Comment Letters: https://www.sec.gov/comments/s7-16-22/s71622.htm
- National Law Review (May 25, 2022): https://www.natlawreview.com/article/fund-any-other-name-sec-proposes-names-rule-amendments?amp

Enhanced Disclosures by Certain Investment Advisers and Investment Companies about Environmental, Social, and Governance Investment Practices

This proposal would:

- Require specific disclosure requirements regarding ESG strategies in fund prospectuses, annual reports, and adviser brochures
- Implement a layered, tabular disclosure approach for ESG funds to allow investors to compare ESG funds at a glance; and
- Require environmentally focused funds to disclose greenhouse gas (GHG) emissions associated with portfolio investments
- Changes would apply to registered investment companies, BDCs (together with registered investment companies, "funds"), registered investment advisers, and certain unregistered advisers (together with registered investment advisers, "advisers")

What does the proposal do?

1) **PROPOSED FUND DISCLOSURES TO INVESTORS**

- The proposed ESG-related disclosure and reporting requirements for registered funds focus on **prospectuses**, **annual shareholder reports**, and **Form N-CEN**. The SEC proposed a new fund taxonomy consisting of three categories of ESG funds, each with accompanying disclosure requirements
  - **Integration Funds**: The SEC defines "Integration Funds" as funds that consider one or more ESG factors alongside other, non-ESG factors in their investment decision-making process, but where such ESG factors are not

dispositive in the funds' investment decisions. For such funds, ESG factors would generally not be given greater weight or consideration than other non-ESG factors in the investment selection process

  - **ESG-Focused Funds**: The SEC defines "ESG-Focused Funds" as funds that consider one or more ESG factors as significant or primary factors in selecting investments or in engagement with portfolio companies. ESG-Focused Funds include, for example, funds that apply inclusionary or exclusionary screens, funds that focus on ESG-related engagement with issuers, and funds that track an ESG-focused index. The category also includes any fund that markets itself as having an ESG focus
  - **Impact Funds**: The SEC defines "Impact Funds" as a subset of ESG-Focused Funds that seek to achieve one or more specific ESG impacts (e.g., advancing the availability of clean water, sustainable management of timberland)

- **Prospectus Disclosures**: Requirement to provide certain additional information about the fund's implementation of ESG factors in its principal investment strategies through a layered disclosure framework. As proposed, **open-end funds** would provide a concise description of this information in the fund's summary prospectus and a more detailed description in the fund's statutory prospectus. For **closed-end funds**, disclosure of summary information would be provided as part of the prospectus's general description of the fund, with the more detailed disclosure presented later in the prospectus
  - **Integration Fund Disclosure**: Integration Funds would be required to explain how they incorporate ESG factors into their investment selection processes and how such ESG factors are considered alongside other factors. In addition, an Integration Fund that considers **greenhouse gas (GHG) emissions** would also be required to disclose additional information about how the fund considers GHG emissions, including the methodology and data sources the fund may use as part of its consideration of GHG emissions
  - **ESG-Focused Fund Disclosure**: ESG-Focused Funds would be required to provide **more detailed disclosure than Integration Funds**, including in a standardized **"ESG Strategy Overview Table"** in the fund's prospectus. Part of the table would consist of a "check-box" format for funds to indicate which common ESG strategies the fund employs (i.e., tracks an index, applies a screen, seeks to achieve a specific impact, proxy voting, engagement, other), while the rest would require brief narrative descriptions of the ESG factor or factors that are the focus of the fund's strategy, how the fund incorporates these ESG factors into its investment decisions, and how the fund votes proxies or otherwise engages with portfolio companies on ESG issues. More detailed descriptions later in the prospectus would address, among other things, any internal methodology or third-party data provider (if applicable) used in selecting investments, identification of indices the fund tracks (if applicable), and the participation of the fund and (as relevant) the fund's adviser in any third-party ESG frameworks (e.g., UN PRI, UN SDG)
  - **Impact Fund Disclosure**: Impact Funds would be required to disclose in their investment objectives **the ESG impact the fund seeks to generate with its investments**, as well as **(1)** how the fund measures progress toward the stated impact, **(2)** the time horizon used to measure that progress, and **(3)** the relationship between the impact the fund is seeking to achieve and the fund's financial returns
- **Annual Shareholder Report Disclosures**: Requirement for funds to include additional ESG-related information in annual shareholder reports. For **registered investment companies**, the proposed disclosure would be included in the management's discussion of fund performance (MDFP) section, and for **BDCs**, in the management discussion and analysis (MD&A) section. These disclosures would include:
  - for **Impact Funds**, a summary of progress towards achieving stated ESG impacts
  - for **ESG-Focused Funds that use proxy voting** as a significant means of implementing an ESG strategy, information regarding how the fund voted proxies on particular ESG-related voting matters
  - for **ESG-Focused Funds that use ESG engagement** as a significant means of implementing an ESG strategy, information regarding the fund's participation in ESG engagement meetings; and
  - for certain **ESG-Focused Funds that consider environmental factors**, GHG emissions metrics
  - *All ESG-Focused Funds, including BDCs, would be required to disclose the carbon footprint and the weighted average carbon intensity (WACI) in their annual shareholder reports unless the fund affirmatively states that it does not consider issuers' GHG emissions as part of its investment strategy in the ESG Strategy Overview Table in the fund's prospectus*

2) ADVISER BROCHURE (FORM ADV PART 2A)

- Proposed ESG-related disclosure and reporting requirements for investment advisers are imposed primarily through amendments to **Form ADV, Part 2A (the Brochure)**
- The Proposed Amendments require investment advisers to disclose with specificity their ESG investing approach by strategy, as well as certain relationships with related persons, and any ESG-related impacts on proxy voting. Disclosure requirements include:
- **ESG Strategy Disclosure**: As proposed, **new sub-Item 8.D** would require advisers to describe the ESG factor(s) considered for each significant investment strategy or method of analysis, including whether and how the adviser incorporates a particular ESG factor and/or a combination of factors into its management of the strategy
  - In addition, similar to registered funds, the proposed disclosure must explain whether and how the adviser employs integration and/or ESG-focused strategies, and if ESG-focused, whether and how the adviser also employs ESG impact strategies. If an adviser considers different ESG factors for different strategies, separate disclosures would be required for each strategy
- **ESG Criteria/Methodology**: Proposed sub-Item 8.D would also require advisers to describe any criteria or methodology used to evaluate, select, or exclude investments based on the consideration of ESG factors, including any:
  1) internal methodology or third-party framework,
  2) inclusionary or exclusionary screen, and/or
  3) index, including the name and a description of how the index utilizes ESG factors
- **Relationships with Related Persons**: Advisers would be required to describe in **Item 10.C of the Brochure** any material relationship or arrangement with any related person that is an ESG consultant or other service provider. The proposed form amendments would not define or otherwise provide guidance regarding the scope or application of the term "ESG consultants or other service providers"
- **Proxy Voting**: If an adviser has specific proxy voting policies and procedures to include one or more ESG considerations when voting client securities, the adviser would be required to describe in **Item 17 of the Brochure** which ESG factors are considered and how they are considered. To the extent this information is previously disclosed in the Brochure (e.g., in Item 8), a cross reference would also satisfy this requirement

3) REGULATORY REPORTING ON FORM N-CEN AND ADV PART 1A

- Proposed form amendments add new reporting requirements to **Form ADV Part 1A**. Amendments would expand current reporting with respect to advisory services provided to **separately managed account (SMA) clients** and private fund to include:
  - **ESG Data for SMAs**: Advisers must indicate using "Yes" / "No" responses whether ESG factors are considered when managing SMA client accounts and, if yes, the type of strategy (i.e., integration, ESG-focused, impact) and the specific factors considered (i.e., environmental, social, and/or governance). Advisers would also be required to disclose whether they follow any third-party ESG frameworks (e.g., UN PRI) in connection with their advisory services, and list any such frameworks by name
  - **ESG Data for Private Funds**: Similar to the proposed reporting for SMA clients (and the information proposed to be collected on Form N-CEN), advisers and exempt reporting advisers would be required to disclose information about the use of ESG factors in managing each reported private fund, including the type of strategy and specific factors considered
  - **ESG-Related Activities and Related Persons**: Advisers and exempt reporting advisers would also be required to disclose whether they conduct other business activities as, or have related persons that are, ESG consultants or other ESG service providers
- ESG-related information reported in Form ADV Part 1A would be provided in an **adviser's annual update** and **would not require updates on an other-than-annual basis**
- *As noted by the SEC, proposed amendments to Part 1A are primarily designed to collect information regarding advisers' use of ESG factors in their advisory business and better facilitate the SEC's risk monitoring initiatives with respect to ESG*

4) COMPLIANCE POLICIES AND PROCEDURES AND MARKETING

The SEC reaffirmed the existing compliance regime established by **Rule 206(4)-7 under the Advisers Act** and **Rule 38a-1 under the 1940 Act** impose certain obligations on investment advisers and registered funds that incorporate ESG factors

- Advisers' and funds' **compliance policies and procedures** should address the accuracy of ESG disclosures made to clients, investors, and regulators and be reasonably designed to ensure portfolios are managed consistently with the ESG-related investment objectives disclosed by the adviser and/or fund
- Regarding **marketing activities**, the SEC also noted that **Rule 206(4)-1 (the Marketing Rule)** and **Rule 206(4)-8 under the Advisers Act** are designed to prevent false or misleading advertisements by advisers, and that these rules clearly prohibit greenwashing by investment advisers

PROPOSED ESG DISCLOSURE REQUIREMENTS FOR FUNDS AND INVESTMENT ADVISERS

	Registered Funds			Investment Advisers
	Summary Prospectus[17]	Statutory Prospectus[18]	Annual Report	ADV Part 2A
Integration Fund/Strategy	Summarize "in a few sentences" how the fund incorporates ESG factors into its investment process, and which factors are considered.	Describe how the fund incorporates ESG factors into its investment selection process, including which ESG factors it considers. Funds that consider GHG emissions as a factor must specifically describe the methodology used to assess portfolio company GHG emissions.	No disclosure required.	For each strategy, describe how ESG factors are incorporated, and which factors are considered. Explain whether and how ESG factors are considered alongside other non-ESG factors. Describe any criteria or methodology used to evaluate, select, or exclude investments based on the consideration of ESG factors (i.e., internal or third-party methodology, screens, or indices).
ESG-Focused Fund/Strategy	Provide key information about the consideration of ESG factors in a standardized "Strategy Overview" table describing: (i) an overview of the fund's ESG strategy, (ii) how the fund incorporates ESG factors in its investment decisions, and (iii) how the fund votes proxies and/or engages with companies about ESG issues.	Describe how the fund incorporates ESG into its investment selection process, including: (i) the index methodology for any index the fund tracks, (ii) any internal methodology used, (iii) the scoring or rating system of any third-party used by the fund, (iv) the factors applied by any inclusionary or exclusionary screen, (v) a description of any third-party ESG framework used, and (vi) a description of the objectives of any engagement activities, whether by voting proxies or otherwise.	If proxy voting is a significant means of implementing the fund's ESG strategy, disclose certain information regarding how the fund voted proxies on ESG issues. If engagement with issuers on ESG issues through means other than proxy voting is a significant means of implementing a fund's ESG strategy, disclose certain information about engagement activities. If the fund considers environmental factors, disclose the aggregated GHG emissions of the portfolio.	For each strategy, describe how ESG factors are incorporated, and which factors are considered. Explain whether and how the strategy focuses on one or more ESG factors. Describe any criteria or methodology used to evaluate, select, or exclude investments based on the consideration of ESG factors (i.e., internal or third-party methodology, screens, or indices).
Impact Fund/Strategy	Include all disclosures required for ESG-Focused Funds. Include in the fund's investment objective the ESG impact(s) the fund seeks to generate with its investments. Disclose (i) how the fund measures progress toward the stated impact(s), (ii) the time horizon used to measure that progress, and (iii) the relationship between the impact(s) sought and the fund's financial return.	Include all disclosures required for ESG-Focused Funds.	Include all disclosures required for ESG-Focused Funds. Additionally, discuss the fund's progress toward achieving its impact(s) during the reporting period in both qualitative and quantitative terms, including the key factors that materially affected the fund's ability to achieve its impact(s).	Include all disclosures required for ESG-Focused Strategies. Additionally, provide an overview of the impact(s) the adviser seeks to achieve and how it seeks to achieve those impact(s) (including how progress is measured, the key performance indicators analyzed, the time horizon, and the relationship between the impact(s) sought and financial returns).

Source: National Law Review

Links to Additional Information

- SEC Press Release, Final Proposal, & Fact Sheet: https://www.sec.gov/news/press-release/2022-92
- Proposal Comment Letters: https://www.sec.gov/comments/s7-17-22/s71722.htm
- National Law Review (May 31, 2022): https://www.natlawreview.com/article/sec-takes-first-step-toward-standardized-esg-disclosures-funds-and-investment

Substantial Implementation, Duplication, and Resubmission of Shareholder Proposals Under Exchange Act Rule 14a-8

The proposed amendments to Exchange Act Rule 14a-8, the shareholder proposal rule, would:

- Revise three of the substantive bases for exclusion of shareholder proposals under the rule: ***the substantial implementation exclusion****; the* ***duplication exclusion****; and* ***the resubmission exclusion***
- Provide greater certainty and transparency to shareholders and companies as they evaluate whether these bases for exclusion would apply to particular proposals; and
- Facilitate communication between shareholders and the companies they own, as well as among a company's shareholders, on important issues

What does the proposal do?

1) **RULE 14a-8(i)(10) – SUBSTANTIAL IMPLEMENTATION**
   - **Rule 14a-8(i)(10)** currently allows companies to exclude a shareholder proposal that "the company has already substantially implemented"
   - The proposed amendments would provide that a proposal may be excluded as substantially implemented if "the company has already implemented the essential elements of the proposal"

2) **RULE 14a-8(i)(11) – DUPLICATION**
   - **Rule 14a-8(i)(11)** currently allows companies to exclude a shareholder proposal that "substantially duplicates another proposal previously submitted to the company by another proponent that will be included in the company's proxy materials for the same meeting"
   - The proposed amendments would specify that **a proposal "substantially duplicates" another proposal if it "addresses the same subject matter and seeks the same objective by the same means"**

3) **RULE 14a-8(i)(12) – RESUBMISSIONS**
   - **Rule 14a-8(i)(12)** currently allows companies to exclude a shareholder proposal that "**addresses substantially the same subject matter as a proposal, or proposals, previously included in the company's proxy materials within the preceding five calendar years**" if the matter was voted on at least once in the last three years and did not receive sufficient shareholder support
   - The proposed amendments would provide that a proposal constitutes a resubmission if it "**substantially duplicates" a prior proposal and specify that, as with the duplication exclusion, a proposal "substantially duplicates" another proposal if it "addresses the same subject matter and seeks the same objective by the same means."**
   - These changes would **align the "resubmission" standard under Rule 14a-8(i)(12) with the "duplication" standard under Rule 14a-8(i)(11)**

Links to Additional Information

- SEC Press Release, Final Proposal, & Fact Sheet: https://www.sec.gov/news/press-release/2022-121
- Proposal Comment Letters: https://www.sec.gov/comments/s7-20-22/s72022.htm
- JD Supra (Jul 14, 2022): https://www.jdsupra.com/legalnews/sec-cuts-key-provisions-of-proxy-3353335/

Amendments to Exemption from National Securities Association Membership

The re-proposal would amend **Rule 15b9-1** by replacing the proprietary trading exemption with more narrow exemptions from Section 15(b)(8). Under the re-proposal, a Commission-registered broker or dealer would be required to join FINRA if it effects securities transactions other than on an exchange of which it is a member unless:

- It is a member of a national securities exchange
- It carries no customer accounts; and
- Such transactions (i) result solely from orders that are routed by a national securities exchange of which the broker or dealer is a member to comply with Rule 611 of Regulation NMS or the Options Order Protection and Locked/Crossed Market Plan; or (ii) are solely for the purpose of executing the stock leg of a stock-option order

The Current Rule *(Source: National Law Review)*

Under Section 15(b)(8) of the Exchange Act, an SEC-registered broker-dealer may not transact in securities unless the firm is a member of a registered national securities association (i.e., FINRA) or effects transactions in securities solely on a national securities exchange of which it is a member. The Rule allows an SEC registered broker-dealer to avoid becoming a FINRA member if it:

- Is a member of an exchange
- Carries no customer accounts; and
- Has annual gross income of no more than $1,000 that is derived from securities transactions effected otherwise than on a national securities exchange of which it is a member (the "*de minimis* allowance")

Income derived with or through another registered broker-dealer does not count towards the de minimis allowance (the "proprietary trading exclusion"). As a result, a proprietary trading firm that meets the conditions above may engage in unlimited proprietary trading off-exchange without having to become a member of FINRA.

What does the proposal do?

1) **ELIMINATION OF THE DE MINIMUS ALLOWANCE AND PROPRIETARY TRADING EXCLUSION**

   - The Commission re-proposes deleting paragraphs (a)(3) and (b) from **Rule 15b9-1** to eliminate the de minimis allowance and proprietary trading exclusion. *(Rule 15b9-1: https://www.law.cornell.edu/cfr/text/17/240.15b9-1)*
   - The re-proposed elimination of the de minimis allowance and proprietary trading exclusion would preclude proprietary trading firms that are registered with the Commission and conduct off-member-exchange securities trading from relying on Rule 15b9-1 as an exemption from Section 15(b)(8)'s Association membership requirement. Therefore, pursuant to **Section 15(b)(8)**, they would be required to become a member of an Association unless they effect transactions in securities solely on an exchange of which they are a member
   - The Commission believes **the de minimis allowance and proprietary trading exclusions are no longer appropriate** and direct Association regulation of broker dealers' off-member-exchange securities trading activity would promote the protection of investors and the public interest
     - The de minimis allowance and proprietary trading exclusion were intended to permit a type of off-exchange activity that no longer occurs today[128]
     - When Rule 15b9-1 and the proprietary trading exclusion were adopted, virtually all trading activity was conducted manually on the floors of national securities exchanges[12]
     - Today, proprietary, cross-market order routing, and trading strategies are a significant component of the markets, and exchange floor-based businesses represent a fraction of market activity. Despite this shift, the de minimis allowance and proprietary trading exclusion have not been adjusted

- **As of April 2022 there were approximately 65 brokers or dealers that were not FINRA members**, including active proprietary trading firms, which accounted for a significant percentage of off-exchange equities and U.S. Treasury securities transaction volumes, as well as a significant amount of transaction volume on exchanges where they are not a member[132]. Under the amended rule, these 65 firms would be required to join FINRA (unless they qualify for one of the amended rule's exceptions)
- Firms that must become FINRA members would become subject to the fees charged by FINRA to all of its member firms

2) NARROWED CRITERIA FOR EXEMPTION FROM ASSOCIATION MEMBERSHIP

- The Commission is proposing to add to **Rule 15b9-1 a new paragraph (c)** that would set forth **two narrow circumstances in which a broker or dealer could continue to be exempt** from Section 15(b)(8)'s Association membership requirement if it effects transactions in securities otherwise than on an exchange of which it is a member[156]

  - **Routing Exemption**: Paragraph **(c)(1) of Rule 15b9-1** would provide an exemption from Association membership if a broker or dealer that meets the criteria of paragraphs (a) and (b) of the rule effects transactions in securities otherwise than on a national securities exchange of which it is a member that **result solely from orders that are routed by a national securities exchange of which it is a member to comply with Rule 611 of Regulation NMS**[157] **or the Options Order Protection and Locked/Crossed Market Plan**[158]

    The proposed routing exemption would serve the purpose of facilitating compliance with intermarket order protection[170]

  - **Stock-Option Order Exemption**: Paragraph **(c)(2) of amended Rule 15b9-1** would provide an exemption from Association membership if a broker or dealer that meets the criteria of paragraphs (a) and (b) of the rule effects transactions in securities otherwise than on a national securities exchange of which it is a member, with or through another registered broker or dealer, that are **solely for the purpose of executing the stock leg of a stock-option order**[176]

    Paragraph (c)(2) also would require a broker or dealer to **establish, maintain, and enforce written policies and procedures** reasonably designed to ensure and demonstrate that such transactions are solely for the purpose of executing the stock leg of a stock-option order

    Broker-dealers would be required to **preserve a copy of its policies and procedures** in a manner consistent with 17 CFR 240.17a-4 until **three years** after the date the policies and procedures are replaced with updated policies and procedures[177]

3) NO FLOOR-MEMBER HEDGING EXEMPTION

- The **2015 Proposal** provided an exemption from FINRA registration for a dealer that is an exchange member, carries no customer accounts, conducts business on the floor of a national securities exchange, and effects transactions off the exchange, for the dealer's own account with or through another registered broker or dealer, that are **solely for the purpose of hedging the risks of its floor-based activity**.[187]
- The Commission proposed that the hedging exemption be limited to a dealer's floor-based trading on a national securities exchange, and understood then that dealers that limit their activities to an exchange's physical trading floor tend to be specialists or floor brokers based on the floor of an individual exchange[188]
- Based on data available to the Commission that was not available in 2015, the Commission believes that no dealers currently trade in a manner that would enable reliance on the hedging exemption as proposed in the 2015 Proposal
- Accordingly, **the re-proposed rule does not include the hedging exemption** included in the 2015 Proposal[189]

4) EFFECTIVE DATE AND IMPLEMENTATION

- The Commission proposes that the compliance date for amended Rule 15b9-1 would be **one year after publication of any final rule in the Federal Register**

Comparison Chart

The below chart compares similarities and differences between the current Rule, the amendments proposed in 2015, and the re-proposed amendments. *Source: https://www.natlawreview.com/article/broker-dealer-proprietary-trading-groups-finra-may-be-your-future*

Any broker or dealer required by Section 15(b)(8) of the Exchange Act to become a member of a registered national securities association (i.e., any SEC-registered broker-dealer that effects transactions in, or attempts to induce the purchase or sale of, securities other than on an exchange of which such firm is a member) shall be exempt from such requirement if it:

Current Rule 15b9-1	2015 Proposal	2022 Re-Proposal
Is a member of a national securities exchange;	Is a member of a national securities exchange;	Is a member of a national securities exchange;
Carries no customer accounts; and	Carries no customer accounts; and	Carries no customer accounts; and
Has annual gross income derived from purchases and sales of securities otherwise than on a national securities exchange of which it is a member in an amount no greater than $1,000, except that: • Such gross income limitation does not apply to income derived from transactions (1) for the dealer's own account with or through another registered broker or dealer; or (2) through the Intermarket Trading System.[5]	Effects transactions in a securities solely on a national securities exchange of which it is a member, except that: • A broker or dealer may effect transactions off the exchange resulting from orders that are routed by a national securities exchange of which it is a member, to prevent trade-throughs on that national securities exchange consistent with Rule 611 of Regulation NMS.	Effects transactions in a securities solely on a national securities exchange of which it is a member, except that: • A broker or dealer may effect transactions in securities otherwise than on a national securities exchange of which the broker or dealer is a member to comply with Rule 611 of Regulation NMS or ***the Options Order Protection and Locked/Crossed Market Plan***.
	• No Stock Option Order Exemption	• A broker or dealer may effect transactions off the exchange resulting from orders that are solely for the purpose of executing the stock leg of a stock-option order.
	• A dealer that conducts business on the floor of a national securities exchange may effect transactions off the exchange, for the dealer's own account with or through another registered broker or dealer, that are solely for the purpose of hedging the risks of its floor-based activities, by reducing or otherwise mitigating the risks thereof (the Floor Member Hedging Exception).	• No Floor Member Hedging Exception

Links to Additional Information

- SEC Press Release, Final Proposal, & Fact Sheet: https://www.sec.gov/news/press-release/2022-133
- Proposal Comment Letters: https://www.sec.gov/comments/s7-05-15/s70515.htm
- National Law Review (Aug 15, 2022): https://www.natlawreview.com/article/broker-dealer-proprietary-trading-groups-finra-may-be-your-future

Rules to Improve Clearing Agency Governance and to Mitigate Conflicts of Interest

The Securities and Exchange Commission proposed to establish new governance requirements for all registered clearing agencies, including requirements:

- For independent directors, the composition of the board of directors, its nominating committee, and risk management committee
- To identify, mitigate, or eliminate conflicts of interest involving directors or senior managers, and also to document such actions
- For policies and procedures that obligate directors to report conflicts of interest
- For policies and procedures for the board to oversee relationships with service providers for critical services; and
- For policies and procedures for the board to solicit, consider, and document the views of participants and relevant stakeholders

What does the proposal do?

The proposed rules would improve governance arrangements across all registered clearing agencies by increasing transparency into clearing agency decision-making, facilitating fair representation of owners and participants, and mitigating the potential effects of conflicts of interest between owners and participants, large and small participants, and direct and indirect participants.

1) **BOARD COMPOSITION AND REQUIREMENTS FOR INDEPENDENT DIRECTORS**

Proposed Rules 17Ad-25(b), (e) and (f): Proposed Rules 17Ad-25(b), (e), and (f) would establish requirements related to **independent directors**. Rule **17Ad-25(b)(1)** would require that a majority of the directors of a registered clearing agency must be independent directors, as defined in proposed Rule 17Ad-25(a)

The proposal also provides that, if a majority of the voting interests issued as of the immediately prior record date are directly or indirectly held by participants, then at least **34 percent** of the members of the board of directors must be independent directors

- **Rule 17Ad-25(a)** would **define an "independent director"** to mean a director that has no material relationship with the registered clearing agency, or any affiliate thereof. Rule 17Ad-25(a) would define **"material relationship"** to mean a relationship, whether compensatory or otherwise, that reasonably could affect the independent judgment or decision-making of the director and includes relationships during a lookback period of one year. Rule 17Ad-25(a) defines **"affiliate"** to mean a person that directly or indirectly controls, is controlled by, or is under common control with the clearing agency
- **Rule 17Ad-25(b)(2)** would require each registered clearing agency to broadly consider all the relevant facts and circumstances on an ongoing basis to **affirmatively determine that a director does not have a material relationship** with the registered clearing agency or an affiliate of the registered clearing agency to qualify as an independent director. In making such determination, a registered clearing agency must:
  - Identify the relationships between a director, the registered clearing agency, any affiliate thereof, along with the circumstances set forth in proposed Rule 17Ad-25(f)
  - Evaluate whether any relationship is likely to impair the independence of the director in performing their duties; and
  - Document this determination in writing
- **Rule 17Ad-25(e)** would require that, if any committee has the authority to act on behalf of the board of directors, the **composition of that committee** must have at least the same percentage of independent directors as is required under these rules for the board of directors, as set forth in proposed paragraph (b)(1)
- **Rule 17Ad-25(f)** would describe certain circumstances that would **exclude a director** from being an independent director. These circumstances include:
  - The director is subject to rules, policies, and procedures by the registered clearing agency that may undermine the director's ability to operate unimpeded, such as removal by less than a majority vote of shares that are entitled to vote in such director's election

- The director, or a family member, has an employment relationship with or otherwise receives compensation, other than as a director, from the registered clearing agency or any affiliate thereof, or the holder of a controlling voting interest of the registered clearing agency
- The director, or a family member, is receiving payments from the registered clearing agency, or any affiliate thereof, or the holder of a controlling voting interest of the registered clearing agency that reasonably could affect the independent judgment or decision-making of the director

Proposed **Rules 17Ad-25(f)(2)-(6)** would be subject to a **lookback period of one year**

Family member would be defined to include any child, stepchild, grandchild, parent, stepparent, grandparent, spouse, sibling, niece, nephew, mother-in-law, father-in-law, son-in-law, daughter-in-law, brother-in-law, or sister-in-law, including adoptive relationships, any person (other than a tenant or employee) sharing a household with the director or a nominee for director, **a trust** in which these persons (or the director or a nominee for director) have **more than fifty percent** of the beneficial interest, **a foundation** in which these persons (or the director or a nominee for director) control the management of assets, and **any other entity** in which these persons (or the director or a nominee for director) own **more than fifty percent** of the voting interests

2) NOMINATING COMMITTEE

- **Rule 17Ad-25(c)(1)** requires each registered clearing agency to establish a **nominating committee** and a written evaluation process whereby such nominating committee shall evaluate individual nominees to serve as directors
- **Rule 17Ad-25(c)(2)** would require that **(i)** independent directors comprise a majority of the nominating committee, and **(ii)** an independent director chair the nominating committee
- **Rule 17Ad-25(c)(3)** requires the nominating committee specify and document fitness standards approved by the board
- **Rule 17Ad-25(c)(4)** would require the nominating committee to document **the outcome of the clearing agency's written evaluation process** in a manner consistent with the nominating committee's written fitness standards. The process would require the nominating committee to:

  i. Take into account each **nominee's expertise, availability, and integrity**, and demonstrate that the board, taken as a whole, has a **diversity of skills, knowledge, experience, and perspectives**

  ii. Demonstrate the nominating committee has considered **whether a particular nominee would complement the other board members**, such that, if elected, the board of directors, taken as a whole, would represent the views of the owners and participants, including a **selection that reflects the range of different business strategies, models, and sizes across participants, as well as the range of customers and clients the participants serve**

  iii. Demonstrate that the nominating committee considered the **views of other stakeholders** who may be impacted by the decisions of the registered clearing agency, including transfer agents, settlement banks, nostro agents, liquidity providers, technology or other service providers; and

  iv. Identify whether each selected **nominee would meet the definition of independent director** and whether each selected nominee has a known **material relationship** with the registered clearing agency or any affiliate thereof, an owner, a participant, or a representative of another type of stakeholder of the registered clearing agency

3) RISK MANAGEMENT COMMITTEE

- **Rule 17Ad-25(d)(1)** would require each registered clearing agency to **establish a risk management committee** (or committees) to assist the board of directors in overseeing the risk management of the registered clearing agency
- Rule 17Ad-25(d)(1) would also require each risk management committee to **reconstitute its membership** on a regular basis and at all times include representatives from the owners and participants of the registered clearing agency
- **Rule 17Ad-25(d)(2)** would require a risk management committee be able to **provide a risk-based, independent, and informed opinion on all matters** presented to it for consideration in a manner that supports the safety and efficiency of the registered clearing agency

4) **CONFLICTS OF INTEREST**

- **Rule 17Ad-25(g)** would require each registered clearing agency to establish, implement, maintain, and enforce written policies and procedures reasonably designed to **identify and document existing or potential conflicts of interest in the decision-making process** involving directors or senior managers of the clearing agency; and document the mitigation or elimination of such conflicts of interest
- **Rule 17Ad-25(h)** would require registered clearing agencies to establish, implement, maintain, and enforce written policies and procedures reasonably designed to require a director to **document and inform the registered clearing agency promptly of the existence of any relationship or interest** that could affect the independent judgment or decision-making of the director

5) **BOARD OBLIGATION TO OVERSEE SERVICE PROVIDERS FOR CRITICAL SERVICES**

- **Rule 17Ad-25(a)** would define the term **"service provider for critical services"** to mean any person that is contractually obligated to the registered clearing agency for the purpose of supporting clearance and settlement functionality or any other purposes material to the business of the registered clearing agency[133]
- **Rule 17Ad-25(i)(1)** would require each registered clearing agency to establish, implement, maintain, and enforce written policies and procedures designed to enable the board to confirm and document that **risks related to critical service providers** are managed in a manner consistent with the clearing agency's risk management framework, and to review senior management's monitoring of relationships with critical service providers
- **Rule 17Ad25(i)(2)** would require each registered clearing agency to establish, implement, maintain, and enforce written policies and procedures reasonably designed to enable the board to approve **policies and procedures that govern the relationship with service providers for critical services**
- **Rule 17Ad-25(i)(3)** would require each registered clearing agency to establish, implement, maintain, and enforce written policies and procedures reasonably designed to enable the board to review and approve **plans for entering into third-party relationships** where the engagement entails being a service provider for critical services to the clearing agency
- **Rule 17Ad-25(i)(4)** would require each registered clearing agency to establish, implement, maintain, and enforce written policies and procedures reasonably designed to enable the board to, through regular reporting to the board by senior management, confirm that senior management takes appropriate **actions to remedy significant deterioration in performance** or **address changing risks or material issues** identified through ongoing monitoring

6) **OBLIGATION TO FORMALLY CONSIDER STAKEHOLDER VIEWPOINTS**

- **Rule 17Ad-25(j)** would require each registered clearing agency to establish, implement, maintain, and enforce written policies and procedures reasonably designed to solicit, consider, and **document its consideration of the views of participants and other relevant stakeholders** of the registered clearing agency regarding material developments in its governance and operations on a recurring basis

7) **CONSIDERATIONS RELATED TO IMPLEMENTATION AND COMPLIANCE**

- The Commission believes it important to establish governance requirements for registered clearing agencies given the potentially significant risks posed by their size, systemic importance, and/or the risks inherent in the products they clear. Therefore, **implementation of any of the requirements in Rule 17Ad-25, if adopted, should be prompt**

  However, the Commission recognizes that **additional time may be warranted** to address any new requirements, if adopted, by both clearing agencies currently registered with the Commission and those entities that intend to register as clearing agencies with the Commission while the rules are being finalized
- **Implementation** of the proposed rules, if adopted, can and should be done in a manner that carries out the fundamental policy goals of the rules while **minimizing burdens and disruptions as much as practicable, including minimizing the prospect of current directors having to resign before their terms expire**
- Implementation would occur pursuant to a **phased-in compliance schedule**. The proposed rules, if adopted, would have a compliance date **180 days** from publication of the final rules in the Federal Register for ***all provisions other than***

proposed Rule 17Ad-25(b)(1), (c)(2), and (e), and **24 months** ***for the independence requirement for the board and board committees under proposed Rule 17Ad-25(b)(1), (c)(2), and (e)***

8) **REGISTERED CLEARING AGENCIES**

- **Rule 17Ad-25 would apply to all registered clearing agencies**. As applicable to proposed Rule 17Ad-25, **a small entity includes**, when used with reference to a clearing agency, a clearing agency that:
  i. compared, cleared, and settled **less than $500 million** in securities transactions during the preceding fiscal year
  ii. had **less than $200 million of funds and securities in its custody or control** at all times during the preceding fiscal year (or at any time that it has been in business, if shorter), and
  iii. is not affiliated with any person (other than a natural person) that is not a small business or small organization[275]
- Based on existing information about the clearing agencies currently registered with the Commission,[276] **the Commission believes that all such registered clearing agencies exceed the thresholds defining "small entities" set out above**. While other clearing agencies may emerge and seek to register as clearing agencies with the Commission, the Commission believes that no such entities would be "small entities" as defined in **Exchange Act Rule 0-10277**

Links to Additional Information

- SEC Press Release, Final Proposal, & Fact Sheet: https://www.sec.gov/news/press-release/2022-138
- Proposal Comment Letters: https://www.sec.gov/comments/s7-21-22/s72122.htm
- National Law Review (Aug 29, 2022): https://www.natlawreview.com/article/sec-proposes-to-clear-clearing-agencies-governance-to-mitigate-directors-potential

SEC/CFTC Joint Proposed Amendments to Form PF to Amend Reporting Requirements for All Filers and Large Hedge Fund Advisers

The **SEC** and the Commodity Futures Trading Commission **(CFTC)** **jointly proposed amendments** to **Form PF**, the confidential reporting form for certain SEC-registered investment advisers to private funds, to:

- Enhance reporting by large hedge fund advisers on qualifying hedge funds
- Enhance reporting on basic information about advisers and the private funds they advise
- Enhance reporting concerning hedge funds
- Amend how advisers report complex structures; and
- Remove aggregate reporting for large hedge fund advisers

What does the proposal do?

1) **PROPOSED AMENDMENTS TO THE GENERAL INSTRUCTIONS**

- **Reporting Master-Feeder Arrangements and Parallel Fund Structures**: Amendments to Form PF would require advisers to report separately each component fund of a master-feeder arrangement and parallel fund structure[17]
  - Currently, Form PF provides advisers with flexibility to respond to questions regarding master-feeder arrangements and parallel fund structures either in the aggregate or separately, as long as they do so consistently throughout

Form PF[19]. However, it has been observed that when some advisers report in aggregate and some advisers report separately, it resulted in obscured risk profiles (e.g., asset size, counterparty exposure, investor liquidity) and made it difficult to compare complex structures, undermining the utility of the data collected

- Accordingly, the proposal would **require an adviser to report each component fund of a master-feeder arrangement and parallel fund structure**, except where a feeder fund invests all its assets in a single master fund and/or "cash and cash equivalents" (i.e., a disregarded feeder fund)[21]
- Additionally, the proposal would **no longer allow advisers to report any "parallel managed accounts,"** (which is distinguished from "parallel fund structure"), except advisers would continue to be required to report the total value of all parallel managed accounts related to each reporting fund[22]

2) PROPOSED AMENDMENTS CONCERNING BASIC INFORMATION ABOUT THE ADVISER AND THE PRIVATE FUNDS IT ADVISES

- **Proposed Amendments to Section 1a of Form PF - Identifying Information**: Section 1a requires an adviser to report **identifying information about the adviser and the private funds it manages**. Proposed are amendments to collect additional identifying information regarding the adviser, its related persons, as well as their private fund assets under management
  - **LEI for advisers and related persons**: Form PF requires advisers to report the LEI for certain entities, if they have one, such as for the reporting fund and parallel funds.[44] Form PF's **current definition of "LEI"** provides, in the case of a financial institution has not been assigned an LEI, advisers must provide the RSSD ID assigned by the National Information Center of the Board of Governors of the Federal Reserve System ("Federal Reserve Board"), if the financial institution has an RSSD ID[45]
  - **The proposal would remove this requirement** and, instead, provide **advisers must not substitute any other identifier** that does not meet the definition of an LEI[46]
  - While Form PF currently requires advisers to provide the LEI for entities such as reporting funds and parallel funds, if the entities have one, it does **not** require advisers to report the LEI for itself and its related persons.[48] The proposal requires advisers to provide the "LEI" for themselves and their "related persons," if they have an LEI[49]
- **Proposed Amendments to Section 1b of Form PF - Concerning All Private Funds**: Section 1b requires advisers to report certain identifying and other basic information about each private fund the adviser manages. The proposal would amend section 1b to **require advisers to report additional identifying information about the private funds they manage as well as the private funds' assets, financing, investor concentration, and performance**
  - **Type of private fund**: The proposed amendments would identify different types of reporting funds better, and help isolate data according to fund type, to allow for more targeted analysis
  - To help prevent reporting errors and help ensure accuracy concerning the reporting fund's type, the proposal would require advisers to **identify the reporting fund by selecting one type of fund from a list**: **hedge fund that is not a qualifying hedge fund, qualifying hedge fund, liquidity fund, private equity fund, real estate fund, securitized asset fund, venture capital fund, or "other"**[54]
  - Additionally, the proposal would require an adviser to indicate whether the reporting fund is a **"commodity pool,"** which is categorized as a hedge fund on Form PF[55]
  - Finally, the proposal would require advisers to report **whether a reporting fund operates as a UCITS or AIF** or markets itself as a money market fund outside the United States, and in which countries (if applicable)[57]
- **Proposed Amendments to Section 1c of Form PF - Concerning All Hedge Funds**: Section 1c requires advisers to report information about the hedge funds they advise. The proposal would require advisers to **report additional information about hedge funds** to provide greater insight into hedge funds' operations and strategies, assist in identifying trends, and improve data quality and data comparability for purposes of systemic risk assessments and to further investor protection efforts

- **Investment Strategies**: The proposal amends how advisers report hedge fund investment strategies.[107] The proposal would require advisers to indicate **which investment strategies best describe the reporting fund's strategies on the last day of the reporting period**, rather than allowing advisers flexibility to report information as of the data reporting date or throughout the reporting period, as Form PF currently provides[108]
- The proposal would also update the **strategy categories** advisers can select to reflect the understanding of hedge fund strategies better and improve data quality and comparability. Included are **more granular categories for equity strategies, such as factor driven, statistical arbitrage, and emerging markets**. Similarly, the proposal includes more granular categories for credit strategies, such as litigation finance, emerging markets, and asset-backed/structured products
- Also proposed is the addition of categories that have become more commonly pursued by hedge funds since Form PF was adopted, such as **categories concerning real estate and digital assets**[109]

- In connection with the proposed amendments, the term **"digital asset"** would be defined as **an asset that is issued and/or transferred using distributed ledger or blockchain technology ("distributed ledger technology"), including, but not limited to, so-called "virtual currencies," "coins," and "tokens."** These types of assets also are commonly referred to as **"crypto assets."**[111] These terms are viewed as synonymous and are proposing the term and definition to be consistent with the SEC's recent statement on digital assets[112]

3) PROPOSED AMENDEMENTS CONCERNING INFORMATION ABOUT HEDGE FUNDS ADVISED BY LARGE PRIVATE FUND ADVISERS

- A private fund adviser must complete **section 2 of Form PF if it had at least $1.5 billion in hedge fund assets** under management as of the last day of any month in the fiscal quarter immediately preceding the adviser's most recently completed fiscal quarter.[134] This section requires additional information regarding the hedge funds these advisers manage, which is tailored to **focus on relevant areas of financial activity that have the potential to raise systemic concerns**
- **Proposed Amendments to Section 2a**
  - **Removal of aggregate reporting**: The proposal eliminates the requirement for large hedge fund advisers to report **certain aggregated information** about the hedge funds they manage[138]

    Based on Form PF data since its adoption, it is found aggregated adviser level information combines funds with different strategies and activities, thus making analyses less meaningful. Aggregation can mask directional exposures of individual funds (e.g., positions held by one fund may appear to be offset by positions held in a different fund)
- **Proposed Amendments to Section 2b**: Section 2b requires a large hedge fund adviser to report certain additional information about any hedge fund it advises that is a qualifying hedge fund[142]

  Section 2b is designed to assist FSOC in monitoring the **composition of hedge fund exposures** over time as well as the liquidity of those exposures. The information also aids FSOC in its monitoring of credit counterparties' unsecured exposure to hedge funds as well as hedge funds' exposure and ability to respond to market stresses and interconnectedness with CCPs

  Amendments to Section 2b would:
  - Enhance, expand, and simplify **investment exposure** reporting
  - Revise open and **large position** reporting
  - Revise borrowing and **counterparty exposure** reporting
  - Revise **market factor effects** reporting; and
  - Make certain other changes designed to streamline and enhance the value of **data collected on qualifying hedge funds** by: **(a)** adding reporting on currency exposure, turnover, country and industry exposure; **(b)** adding new reporting on CCPs; **(c)** streamlining risk metric reporting and collecting new information on investment performance by strategy and portfolio correlation; and **(d)** enhancing portfolio and financing liquidity reporting

4) PROPOSED AMENDMENTS TO ENHANCE DATA QUALITY

- **Reporting of percentages**: The proposal would require that percentages be **rounded to the nearest one hundredth of one percent** rather than rounded to the nearest whole percent
- **Value of investment positions and counterparty exposures**: The proposal would specify how private fund advisers determine **the value of investment positions** (including derivatives) and counterparty exposures

  Some advisers **net legs** of partially offsetting trades when calculating the value of derivatives positions in accordance with internal methodologies, but others do not, resulting in inconsistent reporting that may obscure a fund's risk profile. The proposal would require these trades to be reported independently on a gross basis[238]
- **Reporting of long and short positions**: The proposal would amend the instructions regarding the reporting of long and short positions on Form PF. The adviser would **classify positions based on the following**:
  1) a long position experiences a gain when the value of the market factor to which it relates increases (and/or the yield of that factor decreases), and
  2) a short position experiences a loss when the value of the market factor to which it relates increases (and/or the yield of that factor decreases)
- **Calculating certain derivative values**: The proposal would provide that, **(1)** for calculating the value of interest rate derivatives, "value" means the 10-year bond equivalent, and **(2)** for calculating the value of options, "value" means the delta adjusted notional value (expressed as a 10-year bond equivalent for options that are interest rate derivatives)[240]
  - The amended instruction also provides that in determining the value of these derivatives, advisers should **not net long and short positions or offset trades**, but should **exclude closed-out positions** that are closed out with the same counterparty provided that there is no credit or market exposure to the fund
- **Currency Conversions for Reporting in U.S. Dollars**: The proposal amends **Instruction 15** to clarify that if a question requests a **monetary value**, advisers should provide the information in U.S. dollars as of the data reporting date or other requested date (as applicable) and use a foreign exchange rate for the applicable date

  The proposal also amends that if a question requests a **monetary value for transactional data** that covers a reporting period, advisers should provide the information in U.S. dollars, rounded to the nearest thousand, using foreign exchange rates as of the dates of any transactions to convert local currency values to U.S. dollars[242]

5) PROPOSED ADDITIONAL AMENDMENTS

- Proposal amends **Instruction 14** to allow advisers to request a **hardship exemption** electronically to make it easier to submit a temporary hardship exemption[243]
- The proposal revises the terms **"EEA,"** which Form PF defines as the **European Economic Area** and **"G10,"** which is defined as **The Group of Ten**, to:
  1) remove outdated country compositions and
  2) include an instruction that if the composition of the EEA or G10 changes after the effective date of the proposed amendments to Form PF if adopted, advisers would use the current composition as of the data reporting date

Links to Additional Information

- SEC Press Release, Final Proposal, & Fact Sheet: https://www.sec.gov/news/press-release/2022-141
- Proposal Comment Letters: https://www.sec.gov/comments/s7-22-22/s72222.htm
- National Law Review (Aug 23, 2022): https://www.natlawreview.com/article/sec-cftc-joint-proposed-amendments-introduce-enhanced-private-fund-reporting

SEC Draft Strategic Plan for Fiscal Years 2022 to 2026

The draft strategic plan for fiscal years 2022 to 2026 establishes three primary goals:

- Protecting working families against fraud, manipulation, and misconduct
- Developing and implementing a robust regulatory framework that keeps pace with evolving markets, business models, and technologies; and
- Supporting a skilled workforce that is diverse, equitable, inclusive, and is fully equipped to advance agency objectives

3 Primary Goals

GOAL #1: PROTECT WORKING FAMILIES AGAINST FRAUD, MANIPULATION, AND MISCONDUCT

- **1.1**: Pursue enforcement and examination initiatives focused on identifying and addressing risks and misconduct that affects individual investors
- **1.2**: Enhance the use of market and industry data, particularly to prevent, detect, and enforce against improper behavior
- **1.3**: Modernize design, delivery, and content of disclosures so investors, including in particular retail investors, can access consistent, comparable, and material information to make informed investment decisions

GOAL #2: DEVELOP AND IMPLEMENT A ROBUST REGULATORY FRAMEWORK THAT KEEPS PACE WITH EVOLVING MARKETS, BUSINESS MODELS, AND TECHNOLOGIES

- **2.1**: Update existing SEC rules and approaches to reflect evolving technologies, business models, and capital markets
- **2.2**: Examine strategies to address systemic and infrastructure risks faced by our capital markets and our market participants
- **2.3**: Recognize significant developments and trends in our evolving capital markets and adjust our activities accordingly

GOAL #3: SUPPORT A SKILLED WORKFORCE THAT IS DIVERSE, EQUITABLE, AND INCLUSIVE AND IS FULLY EQUIPPED TO ADVANCE AGENCY OBJECTIVES

- **3.1**: Focus on the workforce to increase capabilities, leverage shared commitment to investors, and promote diversity, equity, inclusion, accessibility, and equality of opportunity
- **3.2**: Promote collaboration within and across SEC offices, including through rotation and detail programs, and maximize telework opportunities
- **3.3**: Enhance the agency's internal control and risk management capabilities, including by the development of a robust and resilient program for dealing with threats to the security, integrity, and availability of the SEC's systems and sensitive data
- **3.4**: Modernize the SEC's technology to enable the mission in a cost-effective, secure, and resilient manner

Links to Additional Information

- SEC Press Release, Strategic Plan, & Request for Comment: https://www.sec.gov/news/press-release/2022-148
- Strategic Plan Comment Letters: https://www.sec.gov/comments/cll-13/cll13.htm
- National Law Review (Aug 31, 2022): https://www.natlawreview.com/article/draft-sec-five-year-strategic-plan-emphasizes-importance-climate-disclosures

SEC Adopts Pay Versus Performance Disclosure Final Rules

The Securities and Exchange Commission adopted final rules implementing the pay versus performance requirement as required by Congress in the Dodd-Frank Act. **The Rule will require**:

- ❖ Registrants to disclose, in proxy or information statements in which executive compensation disclosure is required, how executive compensation actually paid by the registrants related to the financial performance of the registrants over the time horizon of the disclosure

The following was directly sourced from the National Law Review. The entry was posted on Tuesday, August 30, 2022.

Link to full article: https://www.natlawreview.com/article/securities-and-exchange-commission-significantly-expands-executive-compensation

Overview of the Final Rule

1) **NEW ITEM 402(V) OF REGULATION S-K**

- **Application and Operation of Item 402(v) of Regulation S-K**: As proposed, the Rule is adopting the requirement to include the new **Item 402(v) of Regulation S-K** **disclosure in any proxy or information statement for which disclosure under Item 402 of Regulation S-K is required**

  As noted by commenters,[31] placing the **pay-versus-performance information in proxy statements and information statements** will provide shareholders with the pay-versus-performance disclosure in circumstances in which shareholder action is to be taken with regard to an election of directors or executive compensation

  The Final Rules apply to all reporting companies (including business development companies), other than foreign private issuers, registered investment companies, and emerging growth companies

- **Format and Location of Disclosure**: The Rule provides registrants flexibility in determining where in the proxy or information statement to provide the disclosure required. The Rule has adopted the **tabular disclosure format**, with the addition of two new financial performance measures – **net income and the Company-Selected Measure**

2) **TABULAR DISCLOSURE**

- For companies other than smaller reporting companies (SRCs), the Final Rules require a table containing, **for each of the five most recently completed fiscal years**:
  - The company's **Summary Compensation Table** measure of total compensation for the company's **principal executive officer (PEO)** and, as an average, for the company's other **named executive officers (NEOs)**
  - **"Executive compensation actually paid" for the company's PEO**
  - **"Executive compensation actually paid," as an average, for the company's other NEOs**
  - **Total stockholder return (TSR) for the company**
  - **Weighted TSR for the company's peer group**
  - **The company's net income; and**
  - **A financial performance measure chosen by the company (the Company-Selected Measure) that represents the most important financial performance measure the company uses to link executive compensation to the company's performance for the most recently completed fiscal year**

- In fiscal years when a company has **multiple PEOs**, the company must include **separate Summary Compensation Table** total compensation and "executive compensation actually paid" columns for each PEO

- **"Executive compensation actually paid" for a fiscal year** is the total compensation reported in the Summary Compensation Table for that year modified by adjustments to equity award and pension benefit amounts, which according to the National Law Review, *"… will require complex and frequent annual fair valuations for equity awards and actuarial input for pension amounts."*
- The **TSR disclosure** in the table is the value of a **fixed US$100 investment scaled by cumulative total shareholder return** (i.e., the TSR for the first covered fiscal year in the table will represent the TSR over that year and the TSR for the second fiscal year will represent the cumulative TSR over the first and the second fiscal years)
- A company may use as its peer group either the group it uses for purposes of disclosing its performance graph in its Form 10-K, or the group it uses for disclosing its compensation benchmarking practices in its compensation discussion/analysis
- Companies may provide **additional performance measures** as new columns in the table. However, such additional disclosures may not be misleading or obscure the required information, and the additional performance measures may not be presented with greater prominence than the required disclosure

3) RELATIONSHIP DISCLOSURE

- In addition to the tabular disclosure, the Final Rules require:
  - The relationships between executive compensation actually paid to the company's PEO and, on average, its other NEOs and **the company's TSR**
  - The relationships between executive compensation actually paid to the company's PEO and, on average, its other NEOs and **the net income of the company**
  - The relationships between executive compensation actually paid to the company's PEO and, on average, its other NEOs and **the company's Company-Selected Measure**; and
  - The relationships between **the company's TSR and its peer group TSR**, in each case over the company's **five most recently completed fiscal years**
- The relationship disclosure **may be in narrative, graphical, or combined narrative and graphical form**. *For example, the relationship disclosure could include a graph providing executive compensation paid and change in the financial performance measures (TSR, net income, or Company-Selected Measure) on parallel axes and plotting compensation and such measures over the required time period. Alternatively, the required disclosure could include narrative or tabular disclosure showing the percentage change over each year of the required time period in both executive compensation paid and the financial performance measures with a brief discussion of how those changes are related*

4) OTHER PERFORMANCE MEASURE DISCLOSURE

- Companies are required to provide **a list of at least three, and up to seven of their most important financial performance measures used to link executive compensation** actually paid to the company's performance
- **The "most important" determination** is made on the basis of looking only to the most recently completed fiscal year. A company has **the option of including non-financial performance measures** in the list, provided that **(i)** such measures are included in its three to seven most important performance measures, and **(ii)** the company has disclosed at least three (or fewer, if the company only uses fewer) most important financial performance measures
- **Performance measures on the list are not required to be ranked**. A company may present one list used by the company to link compensation actually paid to the company's NEOs to company performance. Alternatively, a company may break up the disclosure into two separate lists: one for the PEO and one for the remaining NEOs
- Any disclosure of performance measures (including in the table discussed above) that are **non-GAAP financial measures** will require disclosure as to how they are calculated from the company's audited financial statements

5) SCALED DISCLOSURE FOR SRCS

- **SRCs must disclose** the required amount for the **three, rather than five, most recently completed fiscal years**, and are not required to disclose weighted TSR for a peer group, disclose a Company-Selected Measure, or make pension related adjustment to their Summary Compensation Table total amounts in order to arrive at *"executive compensation actually paid."*

- **SRCs are not required to provide a description of the relationships between executive compensation** actually paid to the company's PEOs and, on average, its other NEOs and the company's Company-Selected Measure, nor the relationships between the company's TSR and its peer group TSR
- **SRCs are not required to disclose a list of their most important performance measures**, and will have until their third filing with pay-versus-performance disclosure, instead of their first, to provide the required Inline XBRL data

6) **TRANSITION RELIEF**

- **SRCs** are required to provide the new pay-versus-performance disclosure for the **last two fiscal years in their first applicable filing** after the Final Rules took effect, **and three years of disclosure in subsequent filings**
- **All other companies** are required to provide the disclosure for **three fiscal years in their first applicable filing** after the Final Rules becomes effective, and **disclosure for an additional year in each of the two subsequent filings** where disclosure is required

Links to Additional Information

- SEC Press Release, Final Rule: https://www.sec.gov/news/press-release/2022-149
- Fact Sheet: https://www.sec.gov/files/34-95607-fact-sheet.pdf
- National Law Review (Aug 30, 2022): https://www.natlawreview.com/article/securities-and-exchange-commission-significantly-expands-executive-compensation

Proposed Amendments Regarding Rule 10b5-1 and Insider Trading

The proposed amendments to **Rule 10b5-1** would:

- Add new conditions to the availability of the affirmative defense under Exchange Act Rule 10b5-1(c)(1)
- Create new disclosure requirements regarding issuers' insider trading policies and regarding the adopting and termination (including modification) of Rule 10b5-1 and certain other trading arrangements by directors, officers, and issuers
- Create disclosure requirements for executive and director compensation regarding timing of certain equity compensation awards
- Update Forms 4 and 5 to require corporate insiders subject to the reporting requirements of Exchange Act Section 16 to identify transactions made pursuant to a Rule 10b5- 1(c)(1) trading arrangement and to disclose all gifts of securities on Form 4

What does the proposal do?

1) **RULE 10b5-1 & TRADING ARRANGEMENTS**

- Require a Rule 10b5-1 **trading arrangement entered into by officers or directors** to include a **120-day mandatory cooling-off period** before any trading can commence under the trading arrangement after its adoption (including adoption of a modified trading arrangement)[23]
- Require a Rule 10b5-1 **trading arrangement entered into by issuers** to include a **30-day mandatory cooling-off period** before any trading can commence under the trading arrangement after its adoption (including adoption of a modified trading arrangement)
- Require officers and directors to personally certify that they are not aware of material nonpublic information about the issuer or the security when they adopt a Rule 10b5-1 trading arrangement

- Rule 10b5-1(b) provides **if a person is aware of MNPI** when the person trades, that is sufficient to establish a violation
- Rule 10b5-1(c)(1) provides an **affirmative defense** for a trade made under a plan established when **the trader was not aware** of MNPI. 10b5-1(c)(1) does not apply to multiple overlapping Rule 10b5-1 trading arrangements for open market trades in the same class of securities
- Rule 10b5-1(c)(2) provides an **affirmative defense** for a trade made by an entity, where the **individual making the trading decision** is not aware of MNPI and the organization has policies and procedures to prevent misuse of MNPI

2) **DISCLOSURE OF INSIDER TRADING POLICIES AND GRANTS OF EQUITY COMPENSATION AWARDS**

- Require an issuer to **disclose in its Form 10-K or Form 20-F whether or not (and if not, why not) the issuer has adopted insider trading policies** and procedures that govern the purchase, sale, or other disposition of the registrant's securities by directors, officers, and employees that are reasonably designed to promote compliance with insider trading laws, rules, and regulations
- **Disclosures regarding grants of equity compensation awards** such as stock options and stock appreciation rights close in time to the issuer's disclosure of material nonpublic information (incl earnings releases and announcements)
- Prompt disclosure of dispositions by gifts of securities by insiders on Form 4 within **2 business days** after a gift is made

Links to Additional Information

- SEC Press Release, Final Proposal, & Fact Sheet: https://www.sec.gov/news/press-release/2021-256
- Proposal Comment Letters: https://www.sec.gov/comments/s7-20-21/s72021.htm
- Harvard Law School Forum on Corporate Governance (Jan. 17, 2022): https://corpgov.law.harvard.edu/2022/01/17/sec-proposes-major-rule-changes-on-trading-plans-and-corporate-buybacks/

Share Repurchase Disclosure Modernization

This proposal would:

- Require an issuer to provide more timely disclosure on a new Form SR regarding purchases of its equity securities for each day that it, or an affiliated purchaser, makes a share repurchase; and
- Enhance the existing periodic disclosure requirements about these purchases required to be provided in Form 10-K and Form 10-Q for domestic issuers, Form 20-F for foreign filers, and Form N-CSR for registered closed-end funds

What does the proposal do?

1) **PROPOSED FORM SR NEXT DAY REPORTING**

Proposed Form SR would require the following disclosure:

- Date of the repurchase
- Identification of the class of securities purchased
- The total number of shares (or units) purchased, including all issuer repurchases whether or not made pursuant to publicly announced plans or programs

- The average price paid per share (or unit)
- The aggregate total number of shares (or units) purchased on the open market
- The aggregate total number of shares (or units) purchased in reliance on the safe harbor in Exchange Act Rule 10b-18; and
- The aggregate total number of shares (or units) purchased pursuant to a plan intended to satisfy the affirmative defense conditions of Exchange Act Rule 10b5- 1(c)
- The aggregate total number of shares (or units) purchased pursuant to a plan intended to satisfy the affirmative defense conditions of Exchange Act Rule 10b5- 1(c)

2) **ENHANCED PERIODIC DISCLOSURES**

The proposed rules revise **Item 703 of Regulation S-K** and would require **an issuer** to disclose:

- The **objective or rationale** for share repurchases and process or criteria used to determine the amount of repurchases
- Any **policies and procedures** relating to purchases and sales of the issuer's securities by its officers and directors **during a repurchase program**, including any restriction on such transactions
- Whether repurchases were made pursuant to a plan that is intended to satisfy the affirmative defense conditions of Exchange Act Rule 10b5-1(c), and if so, the date that the plan was adopted or terminated; and
- Whether repurchases were made in reliance on the Exchange Act Rule 10b-18 **non-exclusive safe harbor**
- The proposed rules also would require the issuer to check a box indicating whether any of the issuer's officers or directors subject to the reporting requirements under Exchange Act Section 16(a) purchased or sold shares or other units of the class of the issuer's equity securities that is the subject of an issuer share repurchase plan or program within **10 business days** before or after the announcement of such plan or program

Links to Additional Information

- SEC Press Release, Final Proposal, & Fact Sheet: https://www.sec.gov/news/press-release/2021-257
- Proposal Comment Letters: https://www.sec.gov/comments/s7-21-21/s72121.htm
- Harvard Law School Forum on Corporate Governance (Jan. 17, 2022): https://corpgov.law.harvard.edu/2022/01/17/sec-proposes-major-rule-changes-on-trading-plans-and-corporate-buybacks/

As always if you have any questions, please let us know.

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