Wenchi Hu PLLC

Regulatory Recap

February 29, 2024

Happy Leap Day!

Notable Developments:

- **FinCEN proposed new AML/CFT requirements targeting investment advisers**
- **TIAA-CREF settled SEC charges of failure to comply with Regulation Best Interest**
- **Van Eck settled charges with the SEC regarding disclosure failures in connection with the launch of VanEck Social Sentiment ETF**
- **SEC Investment Management Division staff updated FAQ regarding the marketing rules**
- **Trade associations continue to seek modification of SEC Staff Accounting Bulletin 121 to enable banks to provide custody services for crypto assets**
- **ECB blog criticizes Bitcoin as a risky and unsuitable investment despite SEC's Bitcoin ETP approval**
- **SEC proposed inflation adjustment to raise the dollar threshold for qualifying venture capital funds**
- **FINRA adopted new Rule 6151 to require members to submit to FINRA for publication the order routing reports**
- **FINRA adopted amendments to conform its rules to T+1 settlement cycle**

FinCEN proposed new AML/CFT requirements targeting investment advisers.

On February 13, 2024, FinCEN proposed rules that would subject investment advisers registered with the SEC (RIAs) and investment advisers that report to the SEC as exempt reporting advisers (ERAs) to the AML/CFT requirements under the Bank Secrecy Act (BSA), including implementing an AML/CFT program, filing suspicious activity reports (SAR) with FinCEN, keeping records relating to the transmittal of funds and fulfilling other obligations applicable to financial institutions (such as broker-dealers) that are subject to the BSA and FinCEN's implementing regulations. However, the proposed rules do not include requirements for RIAs and ERAs to maintain customer identification programs and identify the beneficial owners of their legal entity clients, which are deferred to a later date. Although RIAs and ERAs currently are not subject to the AML/CFT requirements under the BSA, to the extent that RIAs voluntarily establish an AML/CFT compliance program, such program would be subject to the SEC's examination. The SEC has taken enforcement action against an RIA in the past for failure to enforce its AML policies when the RIA voluntarily adopted such policies.

Enforcement Actions:

- **TIAA-CREF settled SEC charges of failure to comply with Regulation Best Interest.** On February 16, 2024, the SEC announced settled charges against TIAA-CREF Individual & Institutional Services LLC (TIAA-CREF), a registered broker-dealer and a subsidiary of TIAA, regarding TIAA-

CREF's failure to comply with Regulation Best Interest (Reg BI). According to the SEC's order, TIAA-CREF made recommendations to retail customers to open an IRA but failed to disclose to the customers certain conflicts of interest involved and the other available investment option of substantially equivalent, lower-cost share classes of affiliated funds. As a result, 94% of the IRA customers during the relevant period could have avoided more than $900,000 combined in expenses. The SEC found that TIAA-CREF violated the general obligation as well as the disclosure, care and compliance obligations of Reg BI.

- **Van Eck settled charges with the SEC regarding disclosure failures in connection with the launch of VanEck Social Sentiment ETF.** On February 16, 2024, the SEC announced its settlement with Van Eck Associates Corporation (Van Eck) with respect to charges that Van Eck failed to disclose a social media influencer's role and the details of the licensing arrangement with the index provider in the launch of the VanEck Social Sentiment ETF (NYSE: BUZZ) (BUZZ ETF) that tracks the BUZX NextGen AI US Sentiment Leaders Index (BUZZ index) based on positive insights from social media and other data. According to the SEC's order, the BUZZ Index provider had informed Van Eck of its plan to retain a well-known and controversial social media influencer to promote the BUZZ Index in connection with the launch of the BUZZ ETF. To incentivize the influencer's marketing and promotion efforts, the BUZZ Index provider requested a change to the proposed licensing fee structure that would give the index provider a larger percentage of the fee when assets under management of the BUZZ ETF met certain thresholds. Van Eck agreed to the request without disclosing to the independent trustees of the ETF board. The SEC found that Van Eck misrepresented and omitted material information to the ETF board regarding the licensing arrangement with the BUZZ Index provider and the involvement of the influencer. In addition, the SEC also found that Van Eck did not adopt and implement policies and procedures reasonably designed to prevent violations of the Investment Advisers Act of 1940 and the rules thereunder.

In Case You Missed It…

- **SEC Investment Management Division staff updated FAQ regarding the marketing rules.** On February 6, 2024, staff of the Division of Investment Management published updated FAQ regarding Rule 206(4)-1, commonly known as the marketing rules. Notably, the new FAQ clarifies the requirements regarding displaying gross and net performance in advertisements. Specifically, the staff reiterated the requirement in the marketing rules that gross performance shown in an advertisement must be accompanied by a presentation of net performance that has been calculated over the same time period and using the same type of return and methodology as the gross performance. In addition, net performance must be presented in a format designed to facilitate comparison with gross performance.
- **Trade associations continue to seek modification of SEC Staff Accounting Bulletin 121 to enable banks to provide custody services for crypto assets.** On February 14, 2024, the Bank Policy Institute (BPI), the American Bankers Association (ABA), the Financial Services Forum, and the Securities Industry and Financial Markets Association (SIFMA) jointly sent the SEC Chairman Gensler a letter to urge the SEC to modify its Staff Accounting Bulletin No. 121 (SAB 121). SAB

121 was issued on March 31, 2022 with the effective date of April 11, 2022. SAB 121 provides staff's views regarding the accounting for crypto custodians. Specifically, with respect to a crypto custodian's responsibility for safeguarding the crypto assets held for trading platform users, the staff believes that the custodian should present a liability on its balance sheet to reflect its obligation to safeguard the crypt-assets held for platform users. This balance sheet treatment of crypto custody responsibility gives rise to significant capital, liquidity and other costs under the banking prudential regulatory framework and presents a challenge for banking organizations to participate in crypto custody activity (as described in the previous BPI, ABA and SIFMA joint letter to the banking regulators, the SIFMA and ABA joint letter to the SEC's Acting Chief Accountant, and their subsequent update letter). Separately, house representatives Wiley Nickel (D-NC) and Mike Flood (R-NB) co-authored an op-ed to urge the SEC to rescind SAB 121 and also worked with Senator Cynthia Lummis (R-WY) to sponsor a Congressional Review Act resolution to end SAB 121.

- **ECB blog criticizes Bitcoin as a risky and unsuitable investment despite SEC's BTC ETP approval.** A blog published on ECB's website on February 22, 2024 characterized Bitcoin as a failed promise to be a global decentralized digital currency and stated that the SEC's latest approval of spot Bitcoin ETP does not change the fact that Bitcoin is not suitable as an investment. Bitcoin price surged over $60,000 in the last few days.
- **SEC proposed inflation adjustment to raise the dollar threshold for qualifying venture capital funds.** On February 14, 2024, the SEC proposed a rule to raise the dollar threshold to $12 million for a fund to qualify a "qualifying venture capital fund" for purposes of the Investment Company Act.
- **FINRA adopted new Rule 6151 to require members to submit to FINRA for publication the order routing reports.** On February 26, 2024, FINRA published Regulatory Notice 24-05 regarding its adoption of new Rule 6151. Rule 6151 requires every FINRA member that is obligated to provide quarterly public disclosure of its order routing practices for NMS securities under SEC Rule 606(a) (Rule 606(a) Report) to provide such report to FINRA. FINRA will then make all Rule 606(a) Reports available on its website. New Rule 6151 will become effective on June 30, 2024. FINRA members will be required to submit their Q2 2024 Rule 606(a) Reports to FINRA within one month after the end of Q2 2024. In addition, if an introducing firm that routes customer orders to one or more clearing firms for further routing and execution adopts its clearing firms' Rule 606(a) Reports by reference, such introducing firm must provide FINRA with a list of its clearing firms and the hyperlink to the webpage where the introducing firm discloses its clearing firm relationships and adopts the clearing firms' Rule 606(a) Reports by reference, and provide updates to FINRA if the information previously provided changes.
- **FINRA adopted amendments to conform its rules to T+1 settlement cycle.** In anticipation of the May 28, 2024 compliance date of amended SEC Rule 15c6-1 and new Rule 15c6-2 in conection with shortening of settlement cycle from T+2 to T+1, FINRA published Regulatory Notice 24-04 to announce the adoption of amendments to several rules, which will become effective on May 28, 2024 or such later date as the SEC may announce for compliance with the T+1 requirement.