# SECURITIES OPERATIONS

*REGULATORY UPDATE*

A PUBLICATION OF mediant

**November 1, 2020**

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## IN THIS ISSUE

## Take Action Now

### SEC's National Investment Advisers Compliance Seminar To Be Held Virtually

On October 7, 2020, the U.S. Securities and Exchange Commission ("SEC" or "Commission") announced that it had rescheduled its Compliance Outreach Program's national seminar for investment companies and investment advisers to November 19, 2020. The program is intended to help Chief Compliance Officers ("CCOs") and other senior personnel at investment companies and investment advisory firms enhance their compliance programs for the protection of investors. Speakers will include senior representatives from the SEC's Office of Compliance Inspections and Examinations ("OCIE"), Division of Investment Management ("IM"), Enforcement, and the investment adviser industry. Topics will include program priorities in 2020, business continuity and information security, issues regarding conflicts of interest, regulatory hot topics, and topics specific to investment companies. The program will be offered as a live webcast on the SEC's website. Both speakers and attendees will be participating in the program remotely. All live webcast attendees may view the program real-time, access presentation materials, and submit questions to the speakers during the presentation. Registration for the event is not required.

- Agenda: https://www.sec.gov/ocie/compliance-outreach-program-national-seminar-111920
- SEC Compliance Outreach Program: https://www.sec.gov/info/complianceoutreach_ia-funds.htm
- SEC Website: www.sec.gov
- Email questions or requests for information to ComplianceOutreach@sec.gov

## SEC PUBLISHES REPORT ON THE EFFECTS OF COVID-19 ECONOMIC SHOCK ON U.S. CREDIT MARKETS

On October 5, 2020, the SEC released a staff report titled *U.S. Credit Markets: Interconnectedness and the Effects of the COVID-19 Economic Shock*, which focuses on the origination, distribution and secondary market flow of credit across U.S. credit markets. The report identifies the interconnections between banking entities, non-banking entities and intermediaries in the U.S. credit markets and, with that framework as a context, discusses how the COVID-19 economic shock reverberated through the credit markets in March and April 2020. The staff report also addresses how the interconnections in the U.S. credit markets operated as the effects of the COVID-19 pandemic took hold. The principal purpose of the report is to identify and place in context key structural- and flow-related interdependencies in the U.S. credit markets as well as areas of stress revealed by the COVID-19 shock, with an eye toward informing policymakers as they seek to improve the functioning and resilience of our financial markets. Among other key takeaways, the report concludes that: 1) the U.S credit markets have changed significantly in size, structure and function since the 2008 global financial crisis; 2) the credit markets are highly interconnected, which can both accelerate risk transmission and facilitate risk absorption; and 3) the immediate and multi-faceted monetary and fiscal policy actions taken by the Federal Reserve and Congress through the CARES Act were instrumental in ameliorating stress in the credit markets, particularly the short-term funding markets.

**SEC Report:** https://www.sec.gov/files/US-Credit-Markets_COVID-19_Report.pdf
**SEC Chair Remarks:** https://www.sec.gov/files/Letter-from-Clayton-and-Kothari.pdf

## SEC ADOPTS FINAL RULE REGARDING FUND OF FUNDS ARRANGEMENTS

On October 7, 2020, the SEC adopted a new rule and related amendments designed to enact a comprehensive regulatory framework for fund of funds arrangements. According to the SEC, the new rule reflects its decades of experience with fund of funds arrangements and is intended to create a consistent and efficient rules-based regime for the formation and oversight of funds of funds. The SEC staff estimates that approximately 40 percent of all registered funds hold an investment in at least one other fund. Total net assets in mutual funds that invest primarily in other mutual funds have grown to $2.54 trillion in 2019. Retail investors similarly use fund of funds arrangements as a convenient way to allocate and diversify their portfolio through a single, professionally managed investment. The SEC's newly adopted Rule 12d1-4 will allow a fund to acquire the shares of another fund in excess of the limits of the Investment Company Act of 1940, without obtaining an individual exemptive order from the SEC if the funds comply with conditions designed to enhance investor protection. In a related action, the SEC also rescinded Rule 12d1-2, as well as most exemptive relief permitting fund of funds arrangements because the new rule makes them obsolete, with the exception of exemptive relief granted to funds of funds that is outside the scope of the rule.

**Final Rule:** https://www.sec.gov/rules/final/2020/33-10871.pdf
**Effective Date:** 60 days after publication in the Federal Register
**Press Release:** https://www.sec.gov/news/press-release/2020-247

## SEC, CFTC ADOPT FINAL RULE ON SECURITY FUTURES MARGIN

On October 22, 2020, the SEC and the U.S. Commodity Futures Trading Commission ("CFTC") together approved: 1) a joint final rule to harmonize the minimum margin level for security futures held in a futures account with the minimum margin level for security futures held in a securities portfolio margin account; and 2) the issuance of a joint Request for Comment on the portfolio margining of uncleared swaps and non-cleared security-based swaps. The SEC and CFTC have joint rulemaking authority regarding margin requirements for security futures. In 2002, the SEC and CFTC adopted rules establishing margin levels for unhedged security futures at 20 percent. In light of the asymmetry in margin requirements resulting from the 15 percent margin level that had been established for security futures and comparable financial products held in a securities portfolio margin account, the SEC and CFTC adopted the new rule to set the required margin level for each long or short unhedged position in a security future at 15 percent of its current market value. In addition, the final rule would set a 15 percent level for security futures if a securities exchange were to resume security future operations or another exchange were to launch security futures contracts. Currently, there are no security futures contracts listed for trading on U.S. exchanges. The SEC and CFTC jointly requested comment on potential ways to implement portfolio margining of uncleared swaps and non-cleared security-based swaps, including whether there are opportunities to enhance efficiencies, reduce complexity, increase consistency and add resiliency to our financial system through adjustments to current margin rules.

**Final Rule:** https://www.sec.gov/rules/final/2020/34-90244.pdf
**Effective Date:** 30 days after publication in the Federal Register
**Request for Comment:** https://www.sec.gov/rules/other/2020/34-90246.pdf
**Comments Due:** 30 days after publication in the Federal Register
**Press Release:** https://www.sec.gov/news/press-release/2020-264

## SEC UPDATES AUDITOR INDEPENDENCE RULES

On October 16, 2020, the SEC adopted final amendments to certain auditor independence requirements in Rule 2-01 of Regulation S-X. The final Rule modernizes and more effectively focuses the auditor analysis on relationships and services that may pose threats to an auditor's objectivity and independence. The final amendments reflect updates based on recurring fact patterns that SEC staff have observed over years of consultations in which certain relationships and services triggered technical independence rule violations without necessarily impairing an auditor's objectivity and impartiality. These relationships either triggered non-substantive rule breaches or required potentially time-consuming audit committee review of non-substantive matters, thereby diverting time, attention, and other resources of audit clients, auditors, and audit committees from other investor protection efforts. The final amendments feature auditor independence requirements that will be used to evaluate specific relationships and services, with a focus on protecting investors against threats to the objectivity and impartiality of auditors.

**Final Rule:** https://www.sec.gov/rules/final/2020/33-10876.pdf
**Effective Date:** 180 days after publication in the Federal Register
**Press Release:** https://www.sec.gov/news/press-release/2020-261

## SEC PROPOSES TO MODIFY ATS RULES TO CAPTURE GOVERNMENT SECURITIES

On September 28, 2020, the SEC announced a proposal designed to enhance the operational transparency, system integrity, and regulatory oversight for alternative trading systems ("ATSs") that trade government securities as well as repurchase and reverse repurchase agreements on government securities ("Government Securities ATSs"). Under the proposal, all Government Securities ATSs would be required to comply with Regulation ATS. The proposal would apply the investor protections Regulation ATS provides to such entities, such as the requirement to adopt written safeguards and written procedures to protect confidential subscriber information, and enable Commission oversight, including surveillance and examination, of these ATSs. The proposal would also require an ATS with significant market share for U.S. Treasury securities or agency securities to provide fair access to trading on the ATS. The proposal is also designed to increase transparency in the government securities markets by requiring Government Securities ATSs to file comprehensive public disclosures on new Form ATS-G. ATSs have become increasingly important to government securities trading, a market which had average daily trading volume of approximately $835 billion over the final six months of 2019. In addition to the proposed rule, the SEC also published a Concept Release soliciting public comment on the regulatory framework for electronic platforms that trade corporate debt and municipal securities.

**Proposed Rule:** https://www.sec.gov/rules/proposed/2020/34-90019.pdf
**Comments Due:** 60 days after publication in the Federal Register
**Press Release:** https://www.sec.gov/news/press-release/2020-227

## SEC NAMES TIMMONS AS CHIEF OF NEW BANKRUPTCY OFFICE

On October 7, 2020, the SEC announced that Nichola L. Timmons was named Chief of the SEC's newly formed Office of Bankruptcy, Collections, Distributions, and Receiverships within the Division of Enforcement. The new Office is designed to centralize existing functions to achieve efficiencies and maximize results for investors. Among other things, the Office will oversee the process through which the SEC collects outstanding monetary judgments, both in district court and bankruptcy proceedings, and returns money to harmed investors through distributions and the work of court-appointed receivers. In her new role, Timmons will oversee the bankruptcy, collection, distribution, and receivership functions and the staff currently dedicated to those functions. Since 2018, Timmons has served as Supervisory Trial Counsel, leading the SEC's distribution function. Prior to that, Timmons was Assistant Director of Distributions, Logistics, and Services at the SEC from 2013 to 2018, Assistant Chief Litigation Counsel in the SEC's Office of Distributions from 2011 to 2013, and Assistant Chief Litigation Counsel in the SEC's Office of Collections and Distributions from 2008 to 2011. Ms. Timmons joined the SEC as a staff attorney in 1998. Ms. Timmons earned her bachelor's degree magna cum laude in Sociology from Wake Forest University in 1992, her master's degree in Sociology from Northwestern University in 1994, and her law degree from the Georgetown University Law Center in 1998.

**Press Release:** https://www.sec.gov/news/press-release/2020-250

## SEC TAPS KANE AS DIRECTOR OF CORPFIN DISCLOSURE REVIEW PROGRAM

On October 13, 2020, the SEC announced that Jessica S. Kane was named Director of the Division of Corporation Finance's Disclosure Review Program. In her role, Kane will lead the SEC Division of Corporation Finance's important work reviewing transactional, periodic and current reports in furtherance of its mission critical work to promote capital formation and protect investors. Kane will lead initiatives to monitor and enhance the effectiveness, relevancy and transparency of disclosures. Kane had previously served as Director of the Office of Credit Ratings since 2017 tasked with overseeing credit rating agencies registered with the SEC as Nationally Recognized Statistical Rating Organizations ("NRSROs"). Prior to that, Kane served as Director of the SEC's Office of Municipal Securities, where she had previously served as Deputy Director and Senior Special Counsel. Prior to joining the SEC's Office of Municipal Securities, Kane served in the SEC's Office of Legislative and Intergovernmental Affairs. Kane originally joined the SEC in 2007 as an attorney in the SEC's Division's Disclosure Review Program. Kane holds a J.D. from George Mason University School of Law and graduated with honors from Georgetown University. In a simultaneous but separate press release, the SEC announced that Tamara Brightwell was named Deputy Director of the Division of Corporation Finance's Disclosure Review Program.

**Kane Press Release:** https://www.sec.gov/news/press-release/2020-252
**Brightwell Press Release:** https://www.sec.gov/news/press-release/2020-253

## FINRA REQUESTS COMMENT ON PROPOSED AMENDMENTS TO SENIOR INVESTOR PROTECTION RULE

On October 5, 2020, the Financial Industry Regulatory Authority ("FINRA") published Regulatory Notice 20-34, which announced proposed amendments to FINRA Rule 2165 covering the financial exploitation of specified adults, including senior citizens. Rule 2165 is the first uniform national standard for placing temporary holds on disbursements to address suspected financial exploitation. Rule 2165 permits a member firm to place a temporary hold on a disbursement of funds or securities from the account of a "specified adult" customer when the firm reasonably believes that financial exploitation of that adult has occurred, is occurring, has been attempted or will be attempted. A retrospective review of Rule 2165 conducted by FINRA indicated that the rule has been an effective tool in the fight against financial exploitation, but supported amendments to extend the hold period for disbursements from an account and securities transactions in an account in order to further investigate suspected financial exploitation of senior investors. The proposed amendments would allow an additional 30-day temporary holding period, in addition to the current 25-day period provided for in Rule 2165, on disbursements and securities transactions to further address suspected financial exploitation of senior investors when the firm has reported the suspicious activity to a state agency or a court of competent jurisdiction.

**Proposed Rule:** https://www.finra.org/sites/default/files/2020-09/Regulatory_Notice_20-34_Attachment_A.pdf
**Regulatory Notice 20-34:** https://www.finra.org/rules-guidance/notices/20-34
**Comments Due:** December 4, 2020

## FINRA REQUESTS COMMENT ON APPLICATION OF RULES RELATING TO SECURITY-BASED SWAPS

On October 15, 2020, FINRA published Regulatory Notice 20-36, which requests comment on a concept proposal it had published regarding the application of FINRA rules to security-based swaps ("SBS") following the SEC's completion of its rulemaking regarding SBS dealers and major SBS participants. The SEC's rulemaking came as a result of Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act which, among other things, amended the definition of "security" in the Securities Exchange Act of 1934 to expressly encompass SBS. Current FINRA Rule 0180, which is set to expire in September 2021, provides a temporary exception from the application of FINRA rules to SBS, with certain limited exceptions. According to FINRA, it is now considering revising Rule 0180 to replace the general exception from FINRA rules for members engaging in SBS activities with limited, targeted exceptions from certain FINRA rules where FINRA believes application of the rules to SBS activity is infeasible or inappropriate, particularly where members' activities are subject to parallel SEC requirements. Under this concept proposal, Rule 0180 would provide that FINRA rules would generally apply to members' activities and positions with respect to SBS to the extent that a particular rule applies to a member's activities and positions with respect to securities, except as specified in amended Rule 0180. Thus, the current presumption that FINRA rules do not apply to SBS, with certain exceptions, would be flipped, and the presumption going forward would be that FINRA rules apply to SBS, with certain exceptions. FINRA is also considering proposing certain modifications to its financial responsibility and operational rules to conform to the SEC's amended net capital rule and take into account members' SBS activities, as well as a new margin rule specifically applicable to SBS.

**Regulatory Notice 20-36:** https://www.finra.org/rules-guidance/notices/20-36
**Comments Due:** November 16, 2020

## FINRA ALERTS FIRMS TO PHISHING EMAIL REQUESTING A RESPONSE TO FAKE SURVEY

On October 6, 2020, FINRA published Regulatory Notice 20-36, which notifies members of a widespread, ongoing phishing campaign that involves fraudulent emails purporting to be from FINRA asking member firms to complete a survey. The email was sent from the domain "@regulation-finra.org" and was preceded by "info" followed by a number, *e.g.*, info5@regulation-finra.org. FINRA recommends that anyone who clicked on any link or image in the email immediately notify the appropriate individuals in their firm of the incident. The domain of "regulation-finra.org" is not connected to FINRA and firms should delete all emails originating from this domain name. FINRA has requested that the Internet domain registrar suspend services for "regulation-finra.org." In the Notice, FINRA reminds firms to verify the legitimacy of any suspicious email prior to responding to it, opening any attachments or clicking on any embedded links.

**Regulatory Notice 20-35:** https://www.finra.org/rules-guidance/notices/20-35
**Sample of Phishing Email:** https://www.finra.org/sites/default/files/2020-10/Regulatory-Notice-20-35_Attachment_A.pdf

## FINRA PUBLISHES AUTHENTICATION TECHNIQUES TO ASSIST FIRMS IN ENHANCING CYBERSECURITY

On October 15, 2020, FINRA published an Information Notice that provides a non-exhaustive background on authentication techniques for firms to consider in their authentication programs. The authentication process is a key element of a firm's cybersecurity program as it confirms that an authorized user seeking access to a firm's network or systems is who they say they are. The process typically relies on one or more "factors," such as a password or personal identification number ("PIN") code, to provide the authentication. The importance of sound authentication techniques to protect investors' and firms' confidential information has increased in light of: 1) escalating threats to the most commonly used form of authentication (single factor or password-based authentication); and 2) firms responding to the COVID-19 pandemic with work arrangements that typically require registered representatives to log in to their networks from a remote location. Among the several authentication methods included in the Notice, FINRA generally cites multi-factor authentication as an effective practice for firms to enhance their broader cybersecurity programs.

**Information Notice:** https://www.finra.org/rules-guidance/guidance/reports/2018-cybersecurity-report

## FINRA TO CEASE OPERATION OF THE OTCBB

On October 1, 2020, the SEC published for comment a FINRA rule proposal that would expand and enhance the obligations of member firms that operate certain systems that regularly disseminate the quotations of identified broker-dealers in over-the-counter ("OTC") equity securities ("inter-dealer quotation systems"). The proposed rule change would also delete the rules related to, and cease the operation of, the OTC Bulletin Board ("OTCBB"), FINRA's inter-dealer quotation system for use by broker-dealers to publish quotations in eligible OTC equity securities. FINRA states that the OTC marketplace was very different when FINRA, then the National Association of Securities Dealers ("NASD"), first established the OTCBB. At that time, members largely relied on printed, rather than electronic media, for obtaining quotation information. Given technological advancements since 1990 and the subsequent increase in alternative electronic venues with more extensive functionality than the OTCBB, the level of quotation activity occurring on the OTCBB has continued to decline over the past several years and is now nonexistent.

**Notice Release:** https://www.sec.gov/rules/sro/finra/2020/34-90067.pdf

## SEC DELAYS ACTION ON FINRA PROPOSAL TO DELETE OATS RULES

On October 8, 2020, the SEC announced that it had designated a longer period within which to take action on a FINRA proposal to delete its rules related to the Order Audit Trail System ("OATS"). FINRA proposed to delete its OATS-related rules once member firms are effectively reporting to the Consolidated Audit Trail ("CAT") and the CAT's accuracy and reliability meet required standards. The SEC noted that it had received three comment letters regarding the proposal. The SEC designated November 30, 2020 as the date by which it would take action.

**Notice Release:** https://www.sec.gov/rules/sro/finra/2020/34-90129.pdf

## FINRA TO INCREASE FEES

On October 14, 2020, the SEC published for comment a FINRA proposal, effective on filing, to increase its fees. As a not-for-profit self-regulatory organization ("SRO"), FINRA relies upon on a mix of fees to fund its operations and regulatory programs, including the Gross Income Assessment ("GIA"), the Trading Activity Fee ("TAF"), and the Personnel Assessment ("PA"). FINRA is imposing increases to each of the GIA, TAF and PA, as well as member registration and qualification examination fees. As proposed, the fee increases would not take effect until 2022 and would be phased in through 2024, by which it is expected to generate an additional $225 million in annual revenues for FINRA. The fee increases would be proportional and would largely preserve the existing allocation of fees among member firms. The proposed fee increases are designed to better align FINRA's revenues with its costs, while preserving the existing equitable allocation of fees among FINRA members. In its filing, FINRA noted that it has not raised its core member regulatory fees materially since 2010, and has not raised these fees at all since 2013, even though the overall costs of FINRA's operations have exceeded its total revenues for most of the last decade. With respect to expenses, FINRA also noted that its expense growth rate from 2010 through 2019 was less than the rate of inflation and significantly lower than expense growth at member firms. Specifically, FINRA's costs increased by 16 percent cumulatively during the period compared with 42 percent for the industry, while U.S. core inflation grew by 19 percent.

**Notice Release:** https://www.sec.gov/rules/sro/finra/2020/34-90176.pdf
**Comments Due:** November 10, 2020

## FINRA, EXCHANGES TO EXTEND MARKET-WIDE CIRCUIT BREAKER PILOT

In related filings, the SEC published proposals, effective on filing, by FINRA (October 13, 2020), The Nasdaq Stock Market LLC ("Nasdaq") (October 9, 2020), the New York Stock Exchange ("NYSE") and the NYSE American LLC ("NYSE American") (both October 8, 2020) to extend their respective pilot programs related to market-wide circuit breakers in National Market System ("NMS") stocks through October 18, 2021. In 2012, FINRA and all U.S. equity exchanges, including Nasdaq, the NYSE and the NYSE American adopted rules that address the circumstances under which they would halt trading in NMS stocks due to extraordinary market volatility (i.e., market-wide circuit breakers). The resulting market-wide circuit breaker mechanisms implemented by FINRA, Nasdaq and the NYSE were approved by the SEC to operate on a pilot basis and, in April 2019, on a permanent basis. The extension of the pilot period will grant FINRA and the exchanges additional time to work with the SEC and market participants in order to determine whether any additional changes to the market-wide circuit breaker mechanisms should be made before they are made permanent, including consideration of rules and procedures for the periodic testing of the mechanisms with industry participants.

**FINRA Notice Release:** https://www.sec.gov/rules/sro/finra/2020/34-90160.pdf
**Nasdaq Notice Release:** https://www.sec.gov/rules/sro/nasdaq/2020/34-90144.pdf
**NYSE Notice Release:** https://www.sec.gov/rules/sro/nyse/2020/34-90134.pdf
**NYSE American Notice Release:** https://www.sec.gov/rules/sro/nyseamer/2020/34-90135.pdf
**Comments Due:** November 12, 2020 (FINRA); November 5, 2020 (Nasdaq); November 4, 2020 (NYSE/NYSE American)

## NASDAQ TO MODIFY FEES AND CREDITS

On October 13, 2020, the SEC published for comment two Nasdaq proposals, effective on filing, to amend its fees and credits at Equity 7. As proposed, Nasdaq would amend its additional rebate to Qualified Market Maker ("QMM") at Equity 7, Section 114(e), remove a rebate provided through the Nasdaq growth program at Equity 7, Section 114(j), and establish and amend certain credits and fees at Equity 7, Section 118. Currently, Nasdaq provides a rebate of $0.00005 per share executed when a QMM meets certain requirements in Section 114(e). Nasdaq has proposed to amend the rebate to provide $0.000075 per share executed in Tapes A and C, while maintaining the current rebate amount for Tape B in order to incentivize firms to increase their liquidity providing activity on Nasdaq. In addition, Nasdaq currently charges a fee of $0.0020 per share executed to a member entering certain order types that remove liquidity from Nasdaq or that execute in a venue other than Nasdaq and has less than a 75 percent ratio of its order liquidity adding activity to its order total volume. The fee is applicable to Tape A, Tape B and Tape C and only applies to orders submitted with a particular order routing option. Among other changes, Nasdaq is proposing to increase the fee from $0.0020 to $0.0030 per share executed.

**Notice Release:** https://www.sec.gov/rules/sro/nasdaq/2020/34-90164.pdf
**Notice Release:** https://www.sec.gov/rules/sro/nasdaq/2020/34-90163.pdf
**Comments Due:** November 9, 2020

## NYSE TO AMEND PRICE LIST

On October 13, 2020, the SEC published for comment an NYSE proposal, effective on filing, to amend its price list to extend through October 2020 the waiver of equipment and related service charges and trading license fees for NYSE trading floor-based member organizations implemented for April 2020 through September 2020. The proposed rule change is intended to respond to the unprecedented events surrounding the spread of COVID-19. For the months of April, May, June, July, August and September, the NYSE waived the annual telephone line charge of $400 per phone number and the $129 fee for a single line phone, jack, and data jack. The NYSE also waived related service charges, including $161.25 to install a single jack, $107.50 to relocate a jack, $53.75 to remove a jack, $107.50 to install voice or data line, $53.75 to disconnect data line, $53.75 to change a phone line subscriber, and miscellaneous telephone charges billed at $106 per hour in 15 minute increments. The NYSE is proposing to extend the waivers of these fees and charges because its trading floor continues to operate with reduced capacity. In a separate filing published on October 14, 2020, the NYSE proposed to further amend its price list to: 1) extend the period for member organizations to transition to the utilization of ports that connect to the NYSE using Pillar technology; 2) extend the decommission period that begins once the transition period ends; and 3) extend the effective date that the NYSE would prorate the monthly fee for ports activated on or after July 1, 2019.

**Notice Release:** https://www.sec.gov/rules/sro/nyse/2020/34-90161.pdf
**Comments Due:** November 9, 2020
**Notice Release:** https://www.sec.gov/rules/sro/nyse/2020/34-90180.pdf
**Comments Due:** November 10, 2020

## SEC DELAYS ACTION ON NYSE AMERICAN CUBE AUCTION PROPOSAL

On October 14, 2020, the SEC announced that it had designated a longer period within which to take action on an NYSE American proposal to modify Rules 971.1NY and 971.2NY regarding its Customer Best Execution ("CUBE") Auction to provide optional all-or-none functionality for larger-sized orders in both the single-leg and complex CUBE Auctions. The SEC received no comment letters regarding the proposal. The SEC designated December 7, 2020 as the date by which it would take action.

**Notice Release:** https://www.sec.gov/rules/sro/nyseamer/2020/34-90178.pdf

## DTC TO SOLIDIFY PARTICIPANT FUND AS SOURCE OF LIQUIDITY

On October 14, 2020, the SEC published for comment a Depositary Trust Company ("DTC") proposal to amend its Rule 4 to provide expressly that the "Participants Fund" is a liquidity resource that DTC may use to fund a settlement funding gap to complete settlement on a business day, whether the funding gap is the result of a participant's default or otherwise. The Participants Fund is designed to be one of the foundational liquidity resources available to DTC. Rule 4 contains the key provisions specifying the rights, duties and obligations of DTC and its participants with respect to the Participants Fund. Every participant is required to make at least a minimum deposit to the Participants Fund, and participants with higher levels of activity that impose greater liquidity risk to the DTC settlement system have proportionally larger required deposits. The principal purpose of the Participants Fund is, and historically has been, to provide a mutualized liquidity resource to satisfy DTC losses and liabilities attributable to its business conducted for the benefit of its participants. DTC proposed the rule amendment because it recognized over time that a reading of certain provisions in Rule 4 may conflict with the historical purpose of the Participants Fund and it is seeking to remove those ambiguities.

**Notice Release:** https://www.sec.gov/rules/sro/dtc-an/2020/34-90169.pdf
**Comments Due:** November 10, 2020

## MSRB TO AMEND FORM G-32 REQUIREMENTS

On October 22, 2020, the SEC published for comment a proposal by the Municipal Securities Rulemaking Board ("MSRB") to amend MSRB Form G-32 to clarify that brokers, dealers, and municipal securities dealers acting as underwriters in the primary offering of municipal securities are obligated to manually complete three data fields on amended Form G-32 when such fields are applicable to a primary offering. More specifically, the proposed rule change would clarify the method of completing amended Form G-32 for the following three data fields: 1) a bank qualified flag, a yes/no question that indicates whether a bank can deduct a portion of the interest cost of the carry for the municipal securities; 2) a planned amortization class bond flag, a yes/no question that indicates whether the offering is an asset-backed bond payable with a fixed sinking fund schedule; and 3) a put end date entry, a relevant date for offerings of puttable securities.

**Notice Release:** https://www.sec.gov/rules/sro/msrb/2020/34-90248.pdf
**Comments Due:** 21 days after publication in the Federal Register

## Notable Enforcement Actions

*This month regulators concluded a number of high-profile enforcement actions with severe penalties covering a broad range of regulatory and securities law violations.*

A firm agreed to pay more than $2.9 billion in disgorgement, penalties and fees, including more than $1 billion to the SEC, to settle charges that it violated the Foreign Corrupt Practices Act ("FCPA") in connection with the 1Malaysia Development Berhad ("1MDB") bribery scheme. Beginning in 2012, former senior employees of the firm used a third-party intermediary to bribe high-ranking government officials in Malaysia and the Emirate of Abu Dhabi. The SEC found that these bribes enabled the firm to obtain lucrative business from 1MDB, a Malaysian government-owned investment fund, including underwriting approximately $6.5 billion in bond offerings. This action follows the charges brought in December 2019 against one of the firm's managing directors for his role in the 1MDB scheme. (**SEC Case #3-20132**)
https://www.sec.gov/litigation/admin/2020/34-90243.pdf

A firm was censured and agreed to pay a total of $920 million in criminal restitution, forfeiture, disgorgement, penalties and fines to settle charges brought in parallel actions by the SEC, the U.S. Department of Justice, and the CFTC that it fraudulently engaged in manipulative trading of U.S. Treasury Securities. Between April 2015 and January 2016, certain traders on the firm's U.S. Treasuries trading desk employed manipulative trading strategies involving U.S. Treasury cash securities. The order states that the traders placed bona fide orders to buy or sell a particular U.S. Treasury security, while nearly simultaneously placing non-bona fide orders, which the traders did not intend to execute, for the same series of U.S. Treasury security on the opposite side of the market. The order states that the non-bona fide orders were intended to create a false appearance of buy or sell interest, which would induce other market participants to trade against the bona fide orders at prices that were more favorable to the firm than the firm otherwise would have been able to obtain. After the traders secured beneficially priced executions for the bona fide orders, they promptly cancelled the non-bona fide orders. (**SEC Case #3-20094**)
https://www.sec.gov/litigation/admin/2020/33-10858.pdf

A firm was censured and fined $5 million for violating Rule 200(g) of Regulation SHO, in part, due to the structure of its prime brokerage swaps business. The firm hedged synthetic exposure to swaps by purchasing or selling the securities referenced in the swaps, and it separated its hedges into two aggregation units – one holding only long positions, and the other holding only short positions. The firm was able to sell its hedges on the long swaps and mark them as "long" sales without concern for Regulation SHO's short sale requirements. The firm's "long" and "short" units failed to qualify for a Regulation SHO exception permitting broker-dealers to establish aggregation units because they were not independent and did not have separate trading strategies. The units had identical management structures, locations, and business purposes as well as the same strategy or objective. As a result, the firm should have netted the long and short positions of both units together or across the entire broker-dealer and marked the orders as long orders or short based on that netting. The order finds that the failure to do so resulted in the firm improperly marking certain sell orders in violation of Regulation SHO. (**SEC Case #3-20103**)
https://www.sec.gov/news/press-release/2020-238

A firm was censured, fined $350,000, and ordered to pay $201,498, plus interest, in restitution to customers for failing to reasonably supervise the activities of two representatives who recommended that many of their customers invest a substantial portion of their assets at the firm in high-risk energy securities. The findings state that the representatives' conduct generated multiple red flags regarding overconcentration in their customers' accounts that raised suitability concerns that the firm failed to reasonably investigate. The firm's trade-review system issued alerts that customers of the representatives were concentrated in the same low-priced energy security. The firm's written supervisory procedures ("WSPs") addressed how to investigate these alerts, but the firm did not follow its procedures in responding to them. The firm did not review the representatives' other customer accounts for concentration trends, and in certain instances, did not consider contacting customers despite the number of alerts or concerns about whether the customers were aware of the risks associated with concentration. Rather, the firm resolved alerts based on the representatives' uncorroborated assurances that their customers were aware of the concentrations in their accounts. In addition, the firm was aware that the representatives had not documented the concentration suitability determination for certain customers, as the firm's WSPs require, raising a concern regarding the underlying suitability of their recommendations. The firm knew, but did not investigate, that the representatives were moving energy securities from customers' advisory accounts into brokerage accounts to avoid the firm's concentration limits in advisory accounts. In addition, the firm's trade blotters for the representatives consistently evidenced that they were affecting a high volume of sales of the high-risk energy securities in certain of their customers' accounts, but the firm failed to follow-up. (**FINRA Case #2015045713304**)

https://www.finra.org/sites/default/files/fda_documents/2015045713304%20Wells%20Fargo%20Advisors%2C%20LLC%20nka%20Wells%20Fargo%20Clearing%20Services%2C%20LLC%20CRD%2019616%20AWC%20jlg%20%282020-1601252369953%29.pdf

A firm was censured, fined $175,000 and ordered to pay $774,574.08, plus interest, in restitution to customers for failing to reasonably supervise a registered representative who recommended short-term trades of corporate bonds and preferred securities in customer accounts. The representative's trading generated nearly 100 automated alerts reflecting that the trading in these accounts exceeded the firm's thresholds for potentially excessive turnover and cost-to-equity ratios. In response to the alerts, the firm failed to take reasonable steps to review red flags and understand the potential risks and rewards associated with the representative's recommendations, or to determine whether those recommendations were suitable. Instead, the firm discussed the alerts with the representative and contacted the affected customers to confirm whether they were satisfied with the representative and his recommendations. The firm conducted a review of the representative's securities recommendations, and concluded that his recommendations were generating high costs and commissions and the products and investment strategies were costing the clients more money than they were making for the clients. Despite these findings, the firm did not take action to address the representative's trading in his customers' accounts and the affected customer accounts continued to generate alerts for potentially excessive turnover and cost-to-equity ratios. (**FINRA Case #2019063917801**)
https://www.finra.org/sites/default/files/fda_documents/2019063917801%20Morgan%20Stanley%20Smith%20Barney%20LLC%20CRD%20149777%20AWC%20%20VA%20%282020-1599869969493%29.pdf

A firm was censured and fined $125,000 for failing to fully and accurately report its short interest positions in certain foreign-listed securities. The findings state that certain reporting errors resulted from situations where the firm held positions in both the foreign-listed and domestic security in the same proprietary account. In those situations, due to a coding issue, the firm failed to offset the two positions to determine whether it held a short position and the number of shares that should be reported for the dual-listed security. In addition, the firm over-reported one position due to a manual error. The findings also state that the firm failed to report short interest positions in certain foreign-listed securities due to a flawed manual review whereby it failed to recognize that a security that was trading on a foreign market had become dually listed in the United States. Furthermore, the firm failed to report one position because its third-party vendor failed to timely update the firm's data concerning its dual-listed securities. Upon receiving notification from its regulator of the reporting deficiencies, the firm addressed the coding issue and oversight that gave rise to the violations. (**FINRA Case #2015044133101**)
https://www.finra.org/sites/default/files/fda_documents/2015044133101%20Barclays%20Capital%20Inc.%20CRD%2019714%20AWC%20sl%20%282020-1601079567599%29.pdf

A firm was censured, fined $100,000, and required to revise its WSPs for reporting transactions to the Trade Reporting and Compliance Engine ("TRACE") with an incorrect time of trade execution and for reporting transactions to TRACE that it was not required to report. The findings state that the firm's traders or back office personnel manually recorded an incorrect time of trade execution and the firm's system inadvertently reported internal transfers of securities that were not required to be reported to TRACE. The findings also state that, due to manual error, the firm recorded the incorrect time of trade execution on the memorandum of brokerage orders. The findings include that the firm failed to establish and maintain a supervisory system, including WSPs, that was reasonably designed to achieve compliance with TRACE reporting and recordkeeping requirements. The firm's WSPs did not include a review for mismatching execution times, which resulted in its failure to detect its reporting of inaccurate execution times. In addition, the firm did not have a procedure to monitor whether it was reporting information to TRACE that it was not required to report. (**FINRA Case #2017055128201**)
https://www.finra.org/sites/default/files/fda_documents/2017055128201%20BGC%20Financial%2C%20L.P.%20CRD%2019801%20AWC%20sl%20%282020-1599959128680%29.pdf

A firm was censured and fined $37,500 for submitting reports to OATS that could not be matched to related orders routed to exchanges due to data that was omitted, inaccurate, incomplete, or improperly formatted. The findings state that while responding to an inquiry from its regulator, the firm learned of a technical issue in its OATS reporting system provided by a third-party vendor. The firm corrected the problem, but the correction created another technical issue that caused its OATS file to omit a column of data for the route order ID/sent to routed order ID field. Instead of reporting data for each order routed, the firm's OATS reporting system reported data for each execution, resulting in reports in OATS that could not be matched to related orders entered on the exchanges. In addition, the firm's reports omitted other data or contained inaccurate or improperly formatted data. (**FINRA Case #2017053003701**)
https://www.finra.org/sites/default/files/fda_documents/2017053003701%20UBS%20Financial%20Services%20Inc.%20CRD%208174%20AWC%20jlg%20%282020-1600906771733%29.pdf

A firm was censured, fined $60,000 and required to review and revise, as necessary, its written anti-money laundering ("AML") program. The firm failed to establish and implement policies and procedures that were reasonably expected to detect and cause the reporting of potentially suspicious transactions. The findings state that the firm had no system for detecting potential customer insider trading and the firm's written AML procedures did not address the potential issue. The firm knew that certain of its customers were insiders of the securities in which they were trading based on information disclosed to the firm in those customers' new account forms, but the firm's systems did not identify those customers' transactions for AML review. As a result, the firm failed to identify that a customer, a self-identified corporate insider of a microcap issuer, was actively trading the stock of his own company. The firm consequently failed to conduct any investigation or cause the reporting of that potentially suspicious activity. Additionally, the firm failed to implement policies and procedures reasonably expected to detect and cause the reporting of potentially suspicious transactions in microcap securities. (**FINRA Case #2017056561102**)
https://www.finra.org/sites/default/files/fda_documents/2017056561102%20Network%201%20Financial%20Securities%20Inc.%20CRD%2013577%20AWC%20sl%20%282020-1600042775356%29.pdf