



By Bruce Treff,
Managing Director of Regulatory and
Compliance Services

By Chuck Booth,
Director of Regulatory and Compliance Services

Regulatory & Legislative Update – First Quarter 2009

The past quarter has continued to see U.S. government agencies and businesses work together in an unprecedented fashion to solve the current financial crisis. While the previous quarter was focused on the immediate effects of the credit and lending crunch, the first quarter, although still dealing with many of these same issues, began focusing on longer-term remedies. The best example of this is in the money market fund arena. To deal with the current crisis, the U.S. Treasury extended the Money Market Fund Guarantee Program until September 18, 2009. In addition, to address long-term remedies, the Investment Company Institute (ICI)'s Money Market Fund Working Group recommended, and the ICI's Board of Governors endorsed, voluntary compliance with a set of stricter money market fund guidelines by the time the Guarantee Program is set to expire in September.

Another excellent example of this shift is with respect to rules regarding short-sales. The fourth quarter of 2008 saw the Securities and Exchange Commission amend Regulation SHO to provide additional penalties on clearing participants that did not deliver long- or short-sold securities by settlement date, in addition to the Form SH filing requirements and the temporary ban on short-sales of certain financial institutions already in effect. More recently, the SEC proposed a new short-sales rule that would restore, in one form or another, former uptick Rule 10a-1 under the Securities Exchange Act of 1934, as amended (the "1934 Act"). Comments on this new rule are due by June 19, indicating the SEC may be looking to finalize it quickly to replace the temporary rules under

Regulation SHO that are set to expire August 1.

In addition, in February, the Federal Reserve and U.S. Treasury announced the expansion of the Term Asset-Backed Securities Loan Facility (TALF) to generate up to \$1 trillion in new lending for businesses and consumers. The Federal Reserve stated that the expanded TALF program is designed to revitalize the securitization market that has suffered from a lack of demand for asset-backed securities since the financial crisis last fall. Likewise, in January, the SEC issued a temporary exemption from certain provisions of the 1934 Act to facilitate the operation of central counterparties to clear and settle eligible credit default swaps (CDS). The temporary exemption, which is set to expire on September 25, 2009, was the SEC's response to recommendations made by the President's Working Group on Financial Markets to provide oversight to the CDS market.

Another regulatory action aimed at restoring confidence in the nation's financial markets is the SEC's issuance of no-action letter relief to four mutual fund complexes from certain affiliated transaction prohibitions in the Investment Company Act of 1940, as amended, to extend the termination of their money market funds' capital support agreements with affiliates until November 6, 2009. The relief allows the funds additional time to work out their divestments of structured investment vehicles held in their portfolios without creating a fire sale or immediately threatening the funds' \$1.00 NAV.



Other actions during the past quarter currently in the proposal stage that are aimed at helping stabilize the U.S. financial markets included the introduction of the Hedge Fund Transparency Act bill into Congress and proposed guidance to Financial Accounting Standard 157 in the form of FASB Staff Position (FSP) FAS 157-e. The Hedge Fund Transparency Act bill would require hedge funds and private investment funds, including venture capital and private equity funds with \$50 million or more in assets to register with the SEC and file an annual information form. The bill would also require such funds to maintain books and records that the SEC may require and to cooperate with the SEC regarding inspections and requests for additional information. FSP FAS 157-e provides firms with additional guidance to determine whether a market is not active and, therefore, a transaction is distressed in arriving at a securities value. The guidance would reduce FAS 157's emphasis on using observable market transactions to arrive at a security's value when relevant market activity indicated those transactions didn't reflect normal market conditions.

The SEC also finalized one of three rule proposals affecting NRSROs and repropose another. On February 2, the SEC published final rules on amendments it had approved in December that require additional registration and disclosure requirements for NRSROs. Among the new requirements are increased disclosures and, in some cases, prohibitions regarding conflicts of interest, as well as increased transparency regarding how the rating agency arrived at its rating and increased record-keeping requirements to aid in an SEC examination of the NRSRO. At the same time, the SEC repropose rules under section 17 of the 1934 Act that would require disclosure of certain ratings history information and mandatory information sharing by NRSROs rating-structured financed products.

With all this action aimed at restoring the financial markets to normal operating conditions, it would seem like regulators would have little time to address anything else. However, there are a host of other rules addressing various other themes that have compliance dates coming up or that were recently finalized or newly proposed this past quarter. Chief among these is the

new Identity Theft rules that require compliance by May 1. These rules, initially scheduled to require compliance by November 1, 2008, were delayed six months in order to permit mutual funds time to adopt and implement compliant identity theft prevention programs. Similarly, on February 12, Massachusetts announced another delay to its much-maligned new information security law. This time, the Massachusetts Office of Consumer Affairs and Business Regulation came into industry favor by not only announcing the delay of the compliance date under the new rules until January 1, 2010, but by also removing one of its more onerous requirements. Under the amended rules, firms no longer need to seek certifications from their vendors that have access to personal information on Massachusetts' residents. Instead, firms can rely on reasonable steps to verify their service providers have the capacity to protect personal information and are applying appropriate security measures to the information.

And last, but not least, although not requiring compliance until new and amended filings on Form N-1A in 2010, the Summary Prospectus rules became effective on March 31, 2009. The amendments permit funds to meet their prospectus delivery requirements through a new, shortened version of the statutory mutual fund prospectus.

As you can tell, the pace of regulatory action and industry response has continued at an incredible speed during the first quarter of 2009 and shows no signs of slowing down. As industry professionals, it is our constant duty to work diligently toward well-thought-out and meaningful changes to our operational, risk and compliance environments. Hopefully our collective changes will ensure that recent past issues will not happen again.