

KITCES IAR ETHICS CE DAY

# Catching Up On Recent Regulatory Changes

*BOI Reporting, FTC Non-Compete Ban, Marketing Rule Enforcement Actions, Reg S-P Amendments, and Custody Implications Due To SLOAs*

 **KITCES**  
IAR CE DAY

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Advancing Knowledge In Financial Planning . . .

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## Agenda

1. BOI Reporting
2. FTC Non-Compete Ban
3. Marketing Rule Enforcement Actions
4. Reg S-P Amendments
5. Custody Implications Due To SLOAs

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## FinCEN Beneficial Ownership Information Reporting

### Background

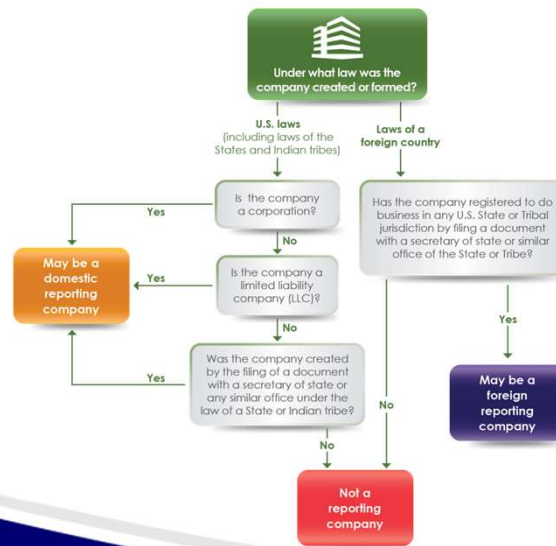
- Originates from the 2021 Corporate Transparency Act
  - Goal: "To make it harder for bad actors to hide or benefit from their ill-gotten gains through shell companies or other opaque ownership structures."
- Promulgated through the Financial Crimes Enforcement Network ("FinCEN"), a bureau of the Department of the Treasury
- Filing of beneficial ownership information ("BOI") regarding companies such as LLCs, corporations, and other entities created by filing a document with a secretary of state ("reporting companies")

### Exemptions

- 23 types of entities are exempt

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## FinCEN Beneficial Ownership Information Reporting



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## FinCEN Beneficial Ownership Information Reporting

Exemption No.	Exemption Short Title
1	Securities reporting issuer
2	Governmental authority
3	Bank
4	Credit union
5	Depository institution holding company
6	Money services business
7	Broker or dealer in securities
8	Securities exchange or clearing agency
9	Other Exchange Act registered entity
10	Investment company or investment adviser
11	Venture capital fund adviser
12	Insurance company
13	State-licensed insurance producer
14	Commodity Exchange Act registered entity
15	Accounting firm
16	Public utility
17	Financial market utility
18	Pooled investment vehicle
19	Tax-exempt entity
20	Entity assisting a tax-exempt entity
21	Large operating company
22	Subsidiary of certain exempt entities
23	Inactive entity

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## FinCEN Beneficial Ownership Information Reporting

### Investment company or investment adviser (Exemption #10)

An entity qualifies for this exemption if **both** of the following criteria apply:

1. The entity is an “investment company” or “investment adviser” defined as either: <ul style="list-style-type: none"> <li>• An investment company in section 3 of the Investment Company Act of 1940 (15 U.S.C. 80a-3); or</li> <li>• An investment adviser in section 202 of the Investment Advisers Act of 1940 (15 U.S.C. 80b-2).</li> </ul>	<input type="checkbox"/> Yes <input type="checkbox"/> No
2. The entity is registered with the Securities and Exchange Commission under either of these authorities: <ul style="list-style-type: none"> <li>• The Investment Company Act of 1940 (15 U.S.C. 80a-1 et seq.); or</li> <li>• The Investment Advisers Act of 1940 (15 U.S.C. 80b-1 et seq.).</li> </ul>	<input type="checkbox"/> Yes <input type="checkbox"/> No

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## FinCEN Beneficial Ownership Information Reporting

### Summary Applicability & Requirements

- Companies that are SEC-registered investment advisers are exempt
  - Companies that are state-registered investment advisers are *not* exempt
- Beneficial Owner: an individual who owns or controls at least 25% of a reporting company or has substantial control over the reporting company
- Beneficial Ownership Information To Be Reported:
  - Full legal name
  - Date of birth
  - Residential street address
  - Identifying # and image of either a U.S. passport, state drivers license, state identification, or, if none of these exist for the beneficial owner, a foreign passport.
- Reporting Company Information To Be Reported:
  - Full legal name, trade name(s), physical address, jurisdiction of formation, and IRS taxpayer ID

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## FinCEN Beneficial Ownership Information Reporting

### Deadlines

- If the reporting company was created before Jan 1, 2024:
  - Jan 1, 2025
- If the reporting company was created on or after Jan 1, 2024:
  - w/in 90 days of company creation
- If the reporting company was created on or after Jan 1, 2025:
  - w/in 30 days of company creation

### Tips

- Beneficial owners (particularly those that own or will own multiple companies) should consider applying for a "FinCEN Identifier" or "FinCEN ID" to submit their FinCEN Identifier in lieu of the BOI that would otherwise need to be reported for each reporting company
- Don't forget to consider holding companies that may own interests in otherwise exempt companies

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## FinCEN Beneficial Ownership Information Reporting

### Hyperlinked Resources:

- [FinCEN BOI Homepage](#)
- [Small Entity Compliance Guide](#)
- [FAQs](#)
- [Reference Materials](#)
- [E-Filing System](#)
- [FinCEN ID Application for Individuals](#)

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## FTC Non-Compete Ban

### Hyperlinked Resources:

- [Final Rule](#)
- [Fact Sheet](#)
- [Worker Notification Model Language](#)
- [Advisor/Client Relationship Equitable Split \(ACRES\) Agreement](#)
- [Plaintiff Press Release](#)

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## Marketing Rule Enforcement Actions

### Be Wary of Hypothetical Performance

- Sept 11, 2023: Settled charges against 9 registered investment advisers
- April 12, 2024: Settled charges against 5 registered investment advisers
- Advertised hypothetical performance on public websites without policies and procedures designed to ensure that the hypothetical performance was “relevant to the likely financial situation and investment objectives of each advertisement’s intended audience” (which is required by the Marketing Rule)
  - Effectively impossible to know the likely financial situation or investment objectives of the entire public → hypothetical performance de facto prohibited for mass audiences or general circulation
- Also cited: false/misleading statements, unsubstantiated statements, and displaying gross performance w/out net performance

### Takeaways

- Take down public / mass-circulation advertisements with hypothetical performance; generally review advertisements for accuracy, substantiation, and Marketing Rule compliance.

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## Marketing Rule Enforcement Actions

### Hyperlinked Resources:

- [2023 SEC Press Release](#)
- [2024 SEC Press Release](#)
- [Marketing Rule](#)
- [Marketing Rule Adopting Release](#)

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## Reg S-P Amendments

### Background & Overview

- Reg S-P governs the treatment of nonpublic personal information of consumers by certain financial institutions (including SEC-registered investment advisers)
  - Hasn't been materially changed since its initial adoption in 2000
  - Also the genesis of the client privacy notice requirement

### New Requirements

- Adopt a written incident response program
  - Reasonably designed to detect, respond to, and recover from unauthorized access to or use of client information
  - Assess the nature and scope of any such incident and to take appropriate steps to contain and control such incidents to prevent further unauthorized access or use
  - Perform due diligence and monitoring of service providers
    - Service provider: "any person or entity that receives, maintains, processes, or otherwise is permitted access to customer information through its provision of services directly to a covered institution."

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## Reg S-P Amendments

### New Requirements (continued)

- Notify affected individuals whose sensitive client information was, *or is reasonably likely to have been*, accessed or used without authorization
  - The notice is to be "clear and conspicuous" and provided as soon as practicable, but not later than 30 days, after awareness
  - The notice is to include details about the incident, the breached data, and how affected individuals can respond to the breach to protect themselves
  - No notice required if the sensitive client information has not been, and is not reasonably likely to be, used in a manner that would result in substantial harm or inconvenience
  - The notice applies solely to "sensitive customer information":
    - "Any component of customer information alone or in conjunction with any other information, the compromise of which could create a reasonably likely risk of substantial harm or inconvenience to an individual identified with the information."
      - In isolation: SSN, DL #, passport #, employer or taxpayer identification #, or biometrics
      - In combination: account #, name, or online user name + the examples above or access code, credit card expiration date, partial social security #, security code, security question/answer, date of birth, place of birth, or mother's maiden name.

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## Reg S-P Amendments

### Effective Date & Compliance Dates

- Effective Date: August 2, 2024
- Compliance Dates:
  - RIAs w/ \$1.5 billion or more in RAUM: 18 months (December 3, 2025)
  - RIAs w/ less than \$1.5 billion in RAUM: 24 months (June 3, 2026)

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## Reg S-P Amendments

### Hyperlinked Resources:

- [Press Release](#)
- [Adopting Release](#)
- [Fact Sheet](#)

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## Custody Implications Due To SLOAs

### Background & Overview

- Custody includes “[a]ny arrangement... under which [an investment adviser is] authorized or permitted to withdraw client funds or securities maintained with a custodian upon [its] instruction to the custodian”
- 2017 SEC No-Action Letter issued to the Investment Adviser Association determined that third party SLOAs trigger custody
  - An investment adviser that does not have discretion as to the amount, payee, and timing of transfers under a SLOA would not implicate the Custody Rule
  - An investment adviser can avoid the annual surprise custody exam if it satisfies 7 conditions
  - Requires reporting in Form ADV Part 1, Item 9

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## Custody Implications Due To SLOAs

**Item 9 Custody**

In this Item, we ask you whether you or a related person has custody of client (other than clients that are investment companies registered under the Investment Company Act of 1940) assets and about your custodial practices.

A. (1) Do you have custody of any advisory clients?

(a) cash or bank accounts?  Yes  No

(b) securities?  Yes  No

If you are registering or registered with the SEC, answer “No” to Item 9.A.(1)(a) and (b) if you have custody solely because (i) you deduct your advisory fees directly from your clients’ accounts, or (ii) a related person has custody of client assets in connection with advisory services you provide to clients, but you have overcome the presumption that you are not operationally independent (pursuant to Advisers Act rule 206(4)-2(d)(5)) from the related person.

(2) If you checked “yes” to Item 9.A.(1)(a) or (b), what is the approximate amount of client funds and securities and total number of clients for which you have custody:

U.S. Dollar Amount	Total Number of Clients
(a) \$ 100,000,000	(b) 100

If you are registering or registered with the SEC and you have custody solely because you deduct your advisory fees directly from your clients’ accounts, do not include the amount of those assets and the number of those clients in your response to Item 9.A.(2). If your related person has custody of client assets in connection with advisory services you provide to clients, do not include the amount of those assets and number of those clients in your response to 9.A.(2). Instead, include that information in your response to Item 9.B.(2).

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**Schedule D - Miscellaneous**

You may use the space below to explain a response to an Item or to provide any other information.

Custody is reported in Item 9A solely due to certain standing letters of authorization that permit the distribution of client funds to third parties. The firm endeavors to comply with the SEC no-action letter to the Investment Adviser Association dated February 21, 2017 in this regard.

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## Custody Implications Due to SLOAs

### The 7 Conditions

- The client provides an instruction to the qualified custodian, in writing, that includes the client's signature, the third party's name, and either the third party's address or the third party's account number at a custodian to which the transfer should be directed.
- The client authorizes the investment adviser, in writing, either on the qualified custodian's form or separately, to direct transfers to the third party either on a specified schedule or from time to time.
- The client's qualified custodian performs appropriate verification of the instruction, such as a signature review or other method to verify the client's authorization, and provides a transfer of funds notice to the client promptly after each transfer.
- The client has the ability to terminate or change the instruction to the client's qualified custodian.
- The investment adviser has no authority or ability to designate or change the identity of the third party, the address, or any other information about the third party contained in the client's instruction.
- The investment adviser maintains records showing that the third party is not a related party of the investment adviser or located at the same address as the investment adviser.
- The client's qualified custodian sends the client, in writing, an initial notice confirming the instruction and an annual notice reconfirming the instruction.

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## Custody Implications Due to SLOAs

### The Key Ambiguity: What Constitutes "Third-Party"?

- First Party: transfers between accounts owned by the same individual(s) or entity(ies)
  - Number of accountholders and SSN(s) / Tax ID(s) must match for both sender and recipient
- Third Party: all other money movements that are not first party
- Examples:
  - Jane Doe IRA <-> Jane Doe individual brokerage account: *first party*
  - Jane & John Doe trust <-> Jane & John Doe joint brokerage account: *first party*
  - Jane Doe IRA <-> Jane & John Doe Trust: *third party*
  - Jane & John Doe joint brokerage account <-> John Doe bank account: *third party*

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## Custody Implications Due To SLOAs

### Hyperlinked Resources:

- [2017 SEC No-Action Letter to the Investment Adviser Association](#)
- [Custody Rule](#)
- [Investment Adviser Association FAQs Regarding the 2017 SEC No-Action Letter to the Investment Adviser Association](#)
- [Schwab SEC Custody Rule No-Action Letter and Additional Guidance](#)
- [New SEC Custody Rule Requirements For Advisors With Third-Party SLOA Authority](#)

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## Want to connect with this presenter?

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