

SEC Issues Guidance on Personal Securities Transactions Reporting

July 1, 2015

On June 26, 2015, the Securities and Exchange Commission (SEC) issued a [guidance update](#) on Rule 204A-1 of the Investment Advisers Act of 1940 (Advisers Act). Rule 204A-1 requires, among other things, certain advisory personnel of a registered investment adviser to report their personal securities transactions to the adviser. This update clarifies when advisory personnel would be deemed to have "no direct or indirect influence or control" over a personal account, such that securities transactions in the account would be exempt from Rule 204A-1's reporting requirements.

Background

Section 204A of the Advisers Act requires registered investment advisers to establish and maintain written policies and procedures reasonably designed to prevent advisers and their employees from misusing material nonpublic information. Under Rule 204A-1, a registered investment adviser must establish and maintain a written code of ethics that requires, among other things, its directors, officers, partners, and any other supervised persons who (i) have access to nonpublic information regarding any clients' purchase or sale of securities or nonpublic information regarding the portfolio holdings of any of the adviser's funds or (ii) are involved in making securities recommendations to clients or who have access to such recommendations that are nonpublic (collectively, Access Persons) to report their personal securities transactions to the adviser. Subsection (b)(3)(i) of the Rule, however, provides that an Access Person would not be required to report personal transactions in an account over which the Access Person has "no direct or indirect influence or control." This exemption (Exemption) would cover, for example, a "blind trust" for which a trustee manages funds for the benefit of an Access Person and over which the Access Person has no right to intervene and no knowledge of the specific portfolio investments made by the trustee.

Guidance Update

As a response to industry inquiries, the update clarifies how the Exemption would apply to arrangements outside of a blind trust, such as (i) a trust managed by a third-party trustee for which an Access Person is a grantor or beneficiary and has limited involvement in the trust affairs or (ii) a personal account managed by a third-party manager who has discretionary investment authority over the account.

According to the update, whether an Access Person may rely on the Exemption with respect to a trust or account would depend on whether the Access Person actually has influence or control (directly or indirectly) over the trust or account. That the Access Person has granted investment authority to a third-party trustee or manager would not, by itself, be sufficient to establish that the Access Person is eligible to rely on the Exemption, given that the Access Person may still suggest or direct investments to the trustee or manager or consult with the trustee or manager as to particular investments. The update suggests that an investment adviser implement controls that look at whether the Access Person actually has direct or indirect influence or control over the trust or account, rather than whether the third-party trustee or manager has discretionary or nondiscretionary investment authority. The investment adviser may, for example:

- Obtain information about a trustee's or manager's relationship to the Access Person (i.e., whether the trustee or manager is an independent professional or friend or relative of the Access Person, and whether the trustee or manager is an affiliated or unaffiliated firm);
- Obtain periodic certifications by the Access Person and the trustee or manager regarding the Access Person's influence or control over the trust or account;
- Provide the Access Person with the exact wording of the Exemption and a clear definition of "no direct or indirect influence or control" that the adviser consistently applies to all Access Persons; and
- On a sample basis, request reports on holdings and transactions in the Access Person's trust or account so as to identify transactions that would have been prohibited under the adviser's code of ethics, absent reliance on the Exemption.

The update also indicates that general certifications by an Access Person would likely be insufficient to establish that the Access Person does not in fact exercise influence or control over a trust or account. Instead, investment advisers should obtain more specific certifications by asking questions such as:

- "Did you suggest that the trustee or third-party discretionary manager make any particular purchases or sales of securities for account X during time period Y?";
- "Did you direct the trustee or third-party discretionary manager to make any particular purchases or sales of securities for account X during time period Y?"; and
- "Did you consult with the trustee or third-party discretionary manager as to the particular allocation of investments to be made in account X during time period Y?"

Registered investment advisers should consider reviewing and updating their code of ethics and any other policies or procedures on personal securities trading in light of the update. Advisers also should consider obtaining additional information and certifications from Access Persons as needed. If you have any questions on the foregoing, please contact your usual Proskauer contact or any of the lawyers listed in this alert.

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