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2021 Annual Review and Outlook for Hedge Funds, Private Equity Funds and Other Private Funds

2021 Proskauer Annual Review and 2022 Outlook for Investment Advisers to Hedge Funds, Private Equity Funds and Other Private Funds

The following annual review (Annual Review) is a summary of some of the significant changes and developments that occurred in the past year and certain recommended practices that investment advisers/investment managers (collectively, advisers) to hedge funds, private equity funds and other private funds (collectively, private funds) should consider when preparing for 2022.

Acknowledgments

This Annual Review is a service to our clients and friends. It is designed only to give general information on the developments actually covered. It is not intended to be a comprehensive summary of recent developments in the law, treat exhaustively the subjects covered, provide legal advice or render a legal opinion.

This Annual Review was prepared by Robert G. Leonard, David J. Marcinkus, Vanessa K. Rakel, Victoria Byler, Vineet Chandra, Peter Gutman, Victoria Hay, Konstantinos Karamanakis, Sara Leonard, Winnie Tong and Caroline Woods, with contributions from:

Michael J. Album, Howard J. Beber, Martin J. Bienenstock, Allan S. Bloom, Ira G. Bogner, Benjamin J. Catalano, John E. Failla, Chantel L. Febus, Robert E. Gaut, Colleen Hart, Vincent Indelicato, Nathan R. Lander, Kirsten Lapham, Jeremy C. Leifer, Michael F. Mavrides, Timothy W. Mungovan, Jeffrey D. Neuburger, Joshua M. Newville, Amanda H. Nussbaum, Stephen Pevsner, Robert E. Plaze, Seetha Ramachandran, Louis E. Rambo, Yong Ren, Jonathan E. Richman, Seth J. Safra, Michael R. Suppappola, David B. Teigman, John Verwey, Samuel J. Waldon, Hadassa Waxman, Christopher M. Wells, Fabio A. Yamada, Frank G. Zarb, John R. Ingrassia, Edward A. Kwalwasser, Adam W. Scoll, Julia Ansanelli, Astrid Champion, Yuna Choi, Amy Gordon, Brooke Gottlieb, Maximilian Greenberg, Jeffrey D. Greenhouse, Joseph Hartunian, Lijuan Hou, Rina Kim, Lucas Kowalczyk, Steve Ma, Tony S. Martinez, Andre Perdiza, Steven Saltz, Jordan Simon, Michael Singh, Jeanette Stecker, Amar Unadkat, Raven Wells-Scott, Ashley Weringa, Susan L. Wiener and Alexa A. Adams.

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SEC Examination Update

The SEC's Division of Examinations (formerly the Office of Compliance Inspections and Examinations, renamed in December 2020) continues to conduct an aggressive inspection program. The SEC reported that it completed 2,952 examinations in its fiscal year 2020, representing approximately 15% of the 13,900 registered investment advisers that it regulates, generally consistent with prior years, and produced over 2,000 deficiency letters. The Division reported that it now has over 1,000 employees.

All examinations are conducted remotely, with relatively short advance warning. Most exams begin with a telephone call announcing the beginning of the exam, followed quickly by a letter requesting documents, typically requesting production within 2 weeks and then telephone calls with selected personnel of the adviser. Since exams are conducted remotely, they do not follow the one-week on-site schedule of prior years and are therefore less predictable in duration, which can range from weeks to months or, on occasion, years.

The examination process has continued to be more targeted and focused on particular risk issues relevant to an adviser. Although SEC exams continue to evolve, and new areas of focus emerge in response to current events and recent developments (such as environmental, social and governance issues (ESG), alternative data and digital assets), many areas of typical focus of exams remain the same. Among the key areas of focus that we have seen in recent examinations, especially examinations of private fund advisers, and that are confirmed by the Division's annual statement of examination priorities and public statements of senior staff, are the following:

- **Material Non-Public Information (MNPI)** – Always a high priority (and one of three main areas noted in the Division's June 2020 Private Fund Risk Alert), examiners will review:
  - trading records for unusually successful trades, trades that do not match a manager's stated investment strategy, and trades that take place around the time of public company announcements;
  - meetings, communications and relationships with public company insiders, and the processes used by compliance personnel to monitor such meetings, communications and relationships;
  - positions held by an investment adviser's personnel on portfolio company or other public or private company boards of directors, creditor committees or other positions providing potential access to non-public information;
  - the use and effectiveness of information barriers;
  - relationships with fund investors whom the SEC refers to as "Value-Added Investors" or "Strategic Investors" (*e.g.*, corporate executives or financial professional investors that have information about investments);
  - the use of restricted lists and trading of companies on restricted lists; and
  - the use of alternative data (see more below).
- **Fees and Expenses** – Examiners focus on issues related to fees and expenses, including:
  - the adequacy of disclosures to clients;
  - the accuracy of fee calculations (see the Division's November 2021 Risk Alert);

- the manner of allocating expenses (including in particular broken-deal expenses) among client and affiliate accounts, especially when client and affiliate accounts participate in co-investments on a side-by-side basis; and
- revenue sharing arrangements with placement agents, broker-dealers, issuers, service providers or other third parties.

- **Conflicts of Interest** – Potential conflicts can include:
  - allocation of investment and trading opportunities;
  - side-by-side management of different client accounts, or different client accounts and proprietary accounts, using the same or similar strategies;
  - arrangements with or services provided by affiliated entities or service providers (and where the approval of any board of directors, advisory board or other third-party consent is requested, the accuracy of relevant disclosures);
  - principal transactions, cross transactions and other transactions where the adviser or any other affiliated party may have an interest (see the Division's July 2021 Risk Alert); and
  - allocation of expenses between the adviser and clients or co-investors.
- **Marketing Materials and Performance Presentations** – Examiners typically review marketing materials carefully for a variety of issues, including:
  - accuracy of statements in marketing materials, and compliance with stated investment guidelines, restrictions or other representations;
  - accuracy of and back-up support for past performance presentations, and compliance with the Investment Advisers Act of 1940 (Advisers Act) performance advertising rules (including providing net returns alongside gross returns);
  - potentially misleading uses of selective examples of past investment performance or recommendations; and
  - use of fund credit lines, whether they have been adequately disclosed, and the effect those lines of credit may have on performance or reported IRR.
- **Cybersecurity** – Questions can include:
  - steps taken to safeguard client assets, accounts and information and prevent account intrusions;
  - due diligence and oversight of vendors and service providers;
  - actions taken in response to events such as ransomware attacks, phishing or account intrusions;
  - controls regarding remote work by employees, including access to online and mobile applications and investor account information;
  - business continuity and disaster recovery plans;

- **Alternative Data** – Questions can include:
  - controls and compliance policies and procedures around the creation, receipt and use of alternative data; and
  - due diligence and oversight of alternative data providers. For more detail, see the "Alternative Data" section in the Annual Report below.
- **ESG** – See the Division's April 2021 Risk Alert, emphasizing:
  - consistency of investment and trading activities with stated policies and procedures;
  - the firm's use of ESG-related terminology, particularly as it relates to adherence with various ESG frameworks or standards; and
  - a review of the firm's written policies and procedures and their implementation, with the expectation that there is compliance oversight of both (i) ESG investing practices and (ii) ESG-related disclosures.
- **Digital Assets** – See the Division's February 2020 Risk Alert, emphasizing:
  - portfolio management and trading practices;
  - custody and safety of client assets;
  - disclosures regarding heightened risks relating to digital assets; and
  - valuation issues.

SEC Enforcement Update

For much of 2021, the SEC has been in transition. In December of 2020, Jay Clayton stepped down as SEC Chairman. Allison Lee then served as the Acting Chair of the SEC until April of 2021, when Gary Gensler was confirmed and sworn in as Chair of the SEC. In June, Gurbir Grewal, who had been the Attorney General of New Jersey, was named the SEC's Director of Enforcement. And in August, Sanjay Wadhwa, who had been the Senior Associate Regional Director for the New York Regional Office of the SEC, was announced as the Deputy Director of Enforcement. Now that the pieces are in place, we expect to see a significant increase in enforcement against private fund managers.

On November 18, 2021, the Division announced its Enforcement Results for Fiscal Year 2021, and there are a few key takeaways.

- In spite of the continued headwinds posed by the global COVID-19 pandemic, the SEC brought 697 enforcement actions in FY 2021. The SEC also filed 434 new enforcement actions, representing a 7% increase over the prior year; 70% of these new or "stand-alone" actions involved at least one individual defendant or respondent.
- Investment adviser and investment company cases accounted for 120 standalone actions in the past year (28% of total new cases, up from 21% in FY2020).
- Insider trading cases accounted for 28 standalone actions in the past year, two fewer than in 2020.
- The SEC also obtained judgments and orders for nearly $2.4 billion in disgorgement and more than $1.4 billion in penalties, which represented a 33% decrease with respect to disgorgement and a 33% increase with respect to penalties as compared to the prior fiscal year.

- The SEC awarded a record amount of whistleblower awards in 2021, awarding a total of $564 million to 108 whistleblowers. The whistleblower program also surpassed $1 billion in awards over the life of the program.

The SEC also highlighted its actions against individuals and gatekeepers and cases involving cryptocurrencies, financial fraud and issuer disclosers, investment professionals, market integrity, insider trading and market manipulation, Foreign Corrupt Practices Act (FCPA), public finance abuse, and securities offerings.

Enforcement Actions Filed in Fiscal Years 2016 to 2021

	FY 2021	FY 2020	FY 2019	FY 2018	FY 2017	FY 2016
Standalone Enforcement Actions (Civil and AP)	434	405	526	490	446	548
Follow-On Admin. Proceedings	143	180	210	210	196	195
Delinquent Filings	120	130	126	121	112	125
Total Actions	697	715	862	821	754	868
Disgorgement and Penalties Ordered (in billions)	$3.80	$4.68	$4.35	$3.95	$3.79	$4.08

Under former Chairman Clayton, private fund advisers benefited indirectly from the SEC's focus on "Main Street" investors. More of the SEC's limited resources were devoted to addressing retail fraud, leaving fewer resources available to focus on private funds. As former Enforcement Director Stephanie Avakian explained recently, the SEC relied more heavily on exams by the Division of Examinations – through deficiency notices and remediation, rather than enforcement actions – to address perceived private fund compliance violations.

The SEC's approach will almost certainly change under the new administration. We expect that Chairman Gensler and Director Grewal will place a far greater emphasis on policing "Wall Street," which today has grown to encompass private funds. As a result, we expect more enforcement actions involving private funds. We expect that "jump ball" type matters that had been resolved under Chairman Clayton with deficiency letters will now find their way to the Enforcement Divison. The past year, particularly the last few months, has given us an idea of what to expect.

Cryptocurrencies

With new types of digital assets and related businesses on the rise, the SEC and other federal authorities have been busy investigating. Chair Gensler has made it abundantly clear that he views regulation and enforcement surrounding cryptocurrencies as a major priority.

In October 2020, multiple high-profile enforcement actions commenced. The SEC charged businessman and computer programmer John McAfee for promoting investments in initial coin offerings (ICOs) to his Twitter followers without disclosing that he was paid to do so. In addition, two separate actions have been

announced by federal prosecutors and the CFTC against BitMEX, one of the world's biggest cryptocurrency trading exchanges. It is alleged that BitMEX failed to limit money laundering and other illegal activities by its customers, despite being aware of such activities. Read more about this matter in our August 27, 2021 blog post here. In the same month, the Attorney-General's Cyber Digital Task Force issued the Cryptocurrency Enforcement Framework, which considers the enforcement challenges arising from the increased uptake of cryptocurrency. This is on the heels of a few years of enforcement actions, particularly those brought by the SEC for unregistered and fraudulent ICOs as well as unregistered crypto-related funds and ICO broker-dealers.

Late last year, the SEC filed a litigated action in the U.S. District Court for the Southern District of New York against Ripple Labs Inc. and two of its executive officers (collectively, "Ripple"), alleging that Ripple raised over $1.3 billion in unregistered offerings of the digital asset known as XRP. The SEC's complaint alleges that, beginning in 2013, Ripple raised funds through the sales of XRP in unregistered securities offerings to investors in the U.S. and abroad. Ripple also allegedly exchanged billions of XRP units for non-cash consideration, including labor and market-making services. The SEC's complaint also named as defendants two executives of Ripple who allegedly effected personal, unregistered sales of XRP totaling approximately $600 million. According to the SEC, during all of this, Ripple failed to register its offers and sales of XRP, or satisfy any exemption from registration, in violation of Section 5 of the Securities Act of 1933 (Securities Act). In its complaint, the SEC argues that XRP is a security under the "Howey Test" because investors who purchased XRP anticipated that profits would be dependent upon Ripple's efforts to manage and develop the market for XRP. Ripple has disputed the SEC's allegations, arguing that XRP is a "fully functioning currency that offers a better alternative to Bitcoin." For more information about this matter, see our February 22, 2021 post here.

Chair Gensler recently asserted that many decentralized finance projects bore enough resemblance to securities that they could and should be subject to regulation by the SEC. In the SEC's first action involving "decentralized finance" (DeFi) technology, two men and their company agreed to settle charges that they improperly offered a decentralized money market product known as DeFi Money Market ("DMM"), through which they sold over $30 million in unregistered securities. The respondents used smart contracts to offer and sell two types of digital tokens, the proceeds of which would then be used to purchase "real world" assets (e.g., car loans) and generate income for the investor. The SEC ultimately found that both types of tokens offered by DMM qualified as securities because they were offered and sold as investment contracts under the *Howey* test. In addition to paying monetary penalties and disgorgement of profits, the respondents were ordered to fund the smart contracts so investors could receive all principal and interest they were owed. For a more detailed summary of this matter, see our August 27, 2021 post here.

Similarly, a web-based trading platform known as Poloniex reached a $10 million settlement with the SEC for operating an unregistered digital asset "exchange" in violation of the Securities Exchange Act of 1934 (Exchange Act). The Poloniex platform allowed users to buy and sell cryptocurrencies and other digital assets. The SEC order noted that even after the SEC issued the DAO Report in July 2017 (providing public guidance on digital assets as securities), Poloniex continued to be "aggressive" in approving new digital assets for trading on its platform. Because the Poloniex platform qualified as an exchange by facilitating transactions of digital asset securities, but failed to register with the SEC, the SEC found Poloniex in violation of Section 5 of the Exchange Act. Please see our August 27, 2021 post here for more information.

SPACs

The SEC will be pursuing a number of enforcement actions involving special purpose acquisition companies (SPACs). For example, in July 2021, the SEC brought an enforcement action against a SPAC, Stable Road Acquisition Company ("Stable Road"), and its major participants based upon false statements by the SPAC target and the SPAC sponsor's failure to conduct appropriate due diligence in the de-SPAC process. Stable Road sought to merge with Momentus Inc., a privately-held space transportation company that plans to offer in-space infrastructure services. The SEC alleged that respondents made materially misleading statements in their public disclosures, as well as misleading statements to their investors, regarding their space technology and certain national security risks. For more information about this action, please see our July 22, 2021 post here. Given the rapid growth in this sector over the past few years, the SEC's Enforcement Division has a working group focused on the area, combined with staff guidance and remarks earlier this year on SPACs relating to the use of projections, accounting methodologies and celebrity involvement with SPACs.

Trading Violations

The SEC continues to bring enforcement actions in connection with trading violations. In August 2021, the SEC announced that it settled charges against Murchinson Ltd., its principal, and its trader, for providing inaccurate information to a hedge fund client's brokers with respect to hundreds of the fund's orders. According to the SEC order, the respondents led the brokers to mismark the sales as "long," which in turn caused the brokers to violate Regulation SHO and to fail to register with the SEC. Respondents all agreed to cease-and-desist orders, and certain respondents agreed to pay penalties and disgorgement of profits with prejudgment interest.

The SEC issued an order in September 2021 stating that it had settled with Helikon, an exempt reporting adviser based in London, for violating Rule 105 of Regulation M of the Exchange Act. Specifically, the company short sold American depositary shares ("ADSs") of NIO, Inc., then purchased NIO ADSs in their public offering three days later, in violation of Rule 105's restriction against purchasing securities in a public offering within five days of short selling those securities (with some limited exceptions that did not apply here). Helikon agreed to a cease-and-desist order, and to pay disgorgement with prejudgment interest and a civil money penalty.

Conflicts of Interest

In September 2021, the SEC announced that it settled with an investment adviser Diastole Wealth Management, Inc. ("Diastole") and its principal for failing to disclose conflicts of interest in connection with their management of investments for a private fund client. The respondents had invested some of the private fund's assets in a company owned and operated by the principal's son. Among various violations of the Advisers Act, the respondents breached their fiduciary duty to the fund and its partners by failing to disclose that the fund was investing in the son's company, and by making material misrepresentations in connection with the same.

Valuation and Pricing

The SEC settled a novel enforcement action in December 2020 against ICE Data Pricing & Reference Data LLC ("ICE"), a pricing service that supplies data to investment managers. The SEC found that from 2015 through 2020, instead of seeking multiple data points, ICE relied upon a single broker quote to determine the prices of certain fixed income securities, making it difficult for ICE clients to ascertain the reliability of the data. The SEC found that ICE failed to develop written compliance policies and procedures that addressed the reliability of single broker quotes, resulting in price quotes that may not

have been "a reasonable reflection of the security's value." In settlement, the SEC found violations of the compliance rule. ICE was ordered to pay an $8 million civil monetary penalty and to cease-and-desist from committing or causing any future violations of the compliance rule. For further details about this matter, see our February 16, 2021 post here.

Fraud and Misleading Disclosures

On February 4, 2021, the SEC announced that it settled with the chief investment officer of International Investment Group, LLC ("IIG"), who allegedly concealed hedge fund portfolio losses by taking certain defaulted loans and inflating their value or replacing them with fake loans, then selling them to advisory clients. The defendant had previously pleaded guilty to counts of securities fraud, wire fraud, and conspiracy to commit several types of fraud in the Southern District of New York ("SDNY") on January 28 (*SEC v. David Hu*, Civil Action Number 20-cv-5496). Additionally, on February 1, a final judgment was entered against him in a civil action brought by the SEC in the Southern District of New York (*U.S. v. David Hu*, Crim. No. 1:20-CR-360), in which Mr. Hu was permanently enjoined from future violations of the federal securities laws' antifraud provisions.

In March 2021, the SEC settled another fraud-related proceeding with principals of the Foundry Capital Group ("FCG"), a state-registered investment adviser that managed the Foundry Mezzanine Opportunity Fund (the "Fund"), finding that they had violated various securities laws by making misrepresentations to clients and failing to disclose conflicts of interest. Specifically, the SEC found that the principals sent, and/or reviewed newsletters to investors containing misstatements and omissions about the "struggling" financial status of companies receiving loans from the Fund. The SEC order additionally found that one respondent had made misrepresentations to investors regarding the valuations of Fund holdings, representing that he would obtain independent valuations but instead valuing them at cost. The order against a principal who was an investment adviser representative found that he failed to disclose to his advisory clients the conflict of interest arising from his sale of interests to the Fund, in which he also had financial interest.

All three principals were subject to cease-and-desist orders. One order included an associational bar but no penalties "in light of [the respondent's] financial condition," while the other principals were subjected to censures and penalties. The adviser representative was further ordered to pay disgorgement and prejudgment interest and to provide notice of the SEC's order to his advisory clients.

In August 2021, the SEC settled with McDonald Partners LLC for failure to disclose to investors in pooled investment vehicle ("PIV") advisory clients that it knew of allegations that investor funds were being misappropriated and used to pay for personal expenses through an individual's debit card. The respondent not only failed to disclose the misappropriation to existing investors, but it continued to raise funds from new investors without disclosing the misappropriation to them, either. The respondent further failed to provide investors in the PIV with audited financial statements or to have an independent public accountant examine the books of the entities involved in the misappropriation. As a result, the SEC found the respondent had violated various antifraud provisions of the federal securities laws and ordered it to cease-and-desist from further violations, be censured, and pay disgorgement, prejudgment interest, and civil penalties.

In another action focusing on fraudulent disclosures, the SEC charged the former principals of TCA Fund Management Group Corp., an advisory firm, in September 2021 for contributing to the firm's "scheme to artificially inflate the net asset values and performance results" of several funds managed by the firm. This case arose out of a previously-settled administrative action against the former COO and CFO of TCA for the same fraudulent scheme. The relevant orders issued in September 2021 found

that the principals caused TCA to inflate net asset values and TCA fund performance by recording in their books non-binding transactions and fraudulent fees, and by including false values and exaggerated performance results in promotional materials. These actions made it appear to investors that the funds always had positive monthly returns, when in fact TCA had at least 34 months of negative returns.

The SEC filed another action in the Northern District of Georgia in August 2021 in connection with a large-scale Ponzi scheme allegedly committed by John Woods and two entities he controls, one an investment adviser and the other an investment fund. The court granted certain of the SEC's requests, including a restraining order, asset freeze, and expedited discovery. The complaint alleges that defendants raised over $110 million from more than 400 investors in 20 states by convincing investors to invest in Woods's investment fund, making various false and misleading statements about the fund's profitability and performance results. The SEC claims Woods and his entities' activities constituted fraud in violation of the federal securities laws. Read more about this matter in the SEC's August 25, 2021 press release here.

SEC Policy and Rulemaking Updates

The SEC has been relatively quiet on the rulemaking front in 2021, especially compared to 2020, which saw a number of rule adoptions affecting private fund advisers. The dearth of rulemaking is likely a result of the change in leadership at the SEC, as Chairman Gary Gensler replaced Jay Clayton in April. We understand that the SEC staff has been busy since the change of administrations preparing rulemaking in accordance with Mr. Gensler's agenda.

There have also been staffing changes at the Division of Investment Management, with the Division's Director, Ms. Dalia Blass, and its Deputy Director and Chief Counsel, Mr. Paul G. Cellupica, concluding their respective tenures in January 2021. Until their permanent replacements are announced, Sarah ten Siethoff, the head of the Division's rulemaking office, is serving as the acting Division Director; Brent Fields, the head of the Division's disclosure review and accounting office, is serving as both the Division's acting Deputy Director and acting Chief Counsel.

Proposed and Adopted Rules

SEC Proposes Enhanced Proxy Voting Reports for Funds and Managers

On Sept. 29, 2021, the SEC proposed new Rule 14Ad-1 under the Exchange Act and amendments to Form N-PX under the Investment Company Act of 1940 (1940 Act). In addition to enhancing proxy reporting by registered investment companies, the proposal would implement Section 951 of Dodd-Frank by requiring all 13F filers (including many private fund managers) to disclose their proxy votes on executive compensation matters ("Say-on-Pay") annually on Form N-PX. Currently, private fund managers are not required to file Form N- PX. Form N-PX is used by registered investment companies to file reports containing their proxy voting records. The proposal also applies to an adviser's decision not to vote, so that each such non-vote on Say-on-Pay matters would also be reported. The comment period for the proposal ends on December 14, 2021.

SEC Increases Advisers Act Qualified Client Thresholds

On June 17, 2021 the SEC issued an order amending Rule 205-3 under the Advisers Act, raising the dollar amount thresholds for qualified clients: (1) from $1,000,000 to $1,100,00 with respect to the

"assets-under-management" test, and (2) from $2,100,000 to $2,200,000 with respect to the "net worth test." The order became effective on August 16, 2021.

Section 205 of the Advisers Act generally prohibits a registered investment adviser from entering into or renewing any investment advisory contract with a client that provides for compensation to the adviser based on a share of capital gains on, or capital appreciation of, the account of a client (a "capital gains performance fee"). Both hedge fund performance fees and private equity fund carried interest allocations are forms of capital gains performance fees covered by Section 205. Rule 205-3 provides an exemption from the general performance-based fee prohibition for advisers to private funds whose investors are "qualified clients" meeting the financial thresholds.

The restriction on performance fees applies to registered advisers only, which excludes, among others, exempt reporting advisers, foreign private advisers, and family offices. The order does not apply retroactively; therefore, contractual relationships with clients entered into before August 16, 2021 will not need to change. For additional information and analysis, please see our client alert.

SEC Revises Marketing Rule for Registered Investment Advisers

On December 22, 2020, the SEC issued a release adopting final rules and rule amendments under the Advisers Act to govern advertisements by registered investment advisers and payments to solicitors. The amendments create a single marketing rule, merging the current advertising rule (Rule 206(4)-1) and cash solicitation rule (Rule 206(4)-3). These amendments codify in many respects the large body of staff interpretations since the advertising rule's adoption in 1961 and the cash solicitation rule's adoption in 1979, and make some significant changes to both rules. The SEC also made related amendments to Form ADV and the books and records rule (Rule 204-2).

Although the rules have already become effective, and advisers can choose to comply with them in advance of the September 2022 compliance date, they do not need to do so until that date.

On October 29, 2021, as discussed in the rules' adopting release, the Division of Investment Management announced that it was rescinding certain staff statements and no-action letters relating to the prior advertising rule.

Definition of Advertisement

The amended definition of "advertisement" contains two prongs: one that captures communications traditionally covered by the advertising rule and another that largely governs solicitation activities previously covered by the cash solicitation rule.

- The first prong relates to any direct or indirect communication that an investment adviser makes that: (i) offers the investment adviser's investment advisory services with regard to securities to prospective clients or private fund investors, or (ii) offers new investment advisory services with regard to securities to current clients or private fund investors. The first prong of the definition covers traditional advertisements and excludes most one-on-one communications tailored to individual private fund investors, and contains certain other exclusions.
- The second prong relates to compensated testimonials and endorsements for which the adviser provides direct or indirect compensation. While capturing some traditional advertisements, this prong is designed primarily to include the activities of advisers' paid solicitors and private funds' placement agents.

The definition of an "advertisement" explicitly extends the scope of the rule to include marketing materials sent to, and solicitation activities directed at, prospective investors in hedge funds, private equity funds, and other private funds managed by an adviser.

The adopting release states that certain information included in a private placement memorandum ("PPM") about the material terms, objectives, and risks of a private fund offering will generally not be an advertisement. However, whether particular additional information included in a PPM constitutes an advertisement of the adviser depends on the relevant facts and circumstances. For example, if a PPM contains related performance information of separate accounts the adviser manages, the PPM would likely be treated as an advertisement and thus would be subject to the provisions of the rule.

Private fund account statements, transaction reports, and other similar materials delivered to existing private fund investors, and presentations to existing clients concerning the performance of private funds in which they have invested (for example, at annual meetings of limited partners) would not be considered advertisements under the marketing rule.

General Prohibitions

The current advertising rule prohibits advertisements that make any untrue statement of a material fact, or omit a material fact necessary to make the statement made, in light of the circumstances under which it was made, not misleading. The new marketing rule retains this traditional anti-fraud provision and adds to the rule six other prohibitions:

- making a material statement of fact that the adviser does not have a reasonable basis for believing it will be able to substantiate upon demand by the SEC;
- including information that would reasonably be likely to cause an untrue or misleading implication or inference to be drawn concerning a material fact relating to the adviser;
- discussing any potential benefits without providing fair and balanced treatment of any associated material risks or limitations;
- referencing specific investment advice provided by the adviser that is not presented in a fair and balanced manner;
- including or excluding performance results, or presenting performance time periods, in a manner that is not fair and balanced; and
- including any information that is otherwise materially misleading.

Use of Performance Information

The marketing rule prohibits, codifies, and expands upon the SEC staff's *Clover Capital* no-action letter. It prohibits any advertisement that contains:

- gross performance, unless the advertisement also presents net performance;
- any performance results, unless they are provided for specific time periods in most circumstances (although this restriction is not generally applicable to private funds);
- any statement that the SEC has approved or reviewed any calculation or presentation of performance results;

- performance results from fewer than all portfolios with substantially similar investment policies, objectives, and strategies to those being offered in the advertisement, with limited exceptions;
- performance results of a subset of investments extracted from a portfolio, unless the advertisement provides, or offers to provide promptly, the performance results of the total portfolio;
- hypothetical performance, unless the adviser adopts and implements policies and procedures reasonably designed to ensure that the hypothetical performance is relevant to the likely financial situation and investment objectives of the intended audience and the adviser provides certain information underlying the hypothetical performance; and
- predecessor performance, unless, among other requirements, there is appropriate similarity with regard to the personnel and accounts at the predecessor adviser and the personnel and accounts at the advertising adviser, and the adviser includes all relevant disclosures clearly and prominently in the advertisement.

Additional Revisions

- *Testimonials and Endorsements* – The new rule prohibits advisers from including a testimonial in an advertisement or directly or indirectly compensating persons who provide testimonials or endorsements without complying with certain disclosure, oversight, and disqualification provisions, which are largely drawn from the existing cash solicitation rule.
- *Third-Party Ratings* – The marketing rule allows the use of third-party ratings in an advertisement, provided the adviser provides disclosures and satisfies certain criteria pertaining to the preparation of the rating.

As mentioned above, the Adopting Release also makes corresponding amendments to the books and records rule and Form ADV. For additional information and analysis, please see our client alert.

Policy Updates

Principal and Cross Trading – On July 21, 2021, the Division of Examinations issued a risk alert on principal and cross trading practices by investment advisers. The Risk Alert notes that principal and cross trading implicates a variety of legal obligations under the Advisers Act, in particular an adviser's fiduciary duty to its clients. Although the Risk Alert does not provide any new insight into the legal or regulatory issues around principal or cross trading practices, it serves as a useful reminder that this remains an area of focus by Division staff.

The Risk Alert is based on the staff's observations as part of an initiative of over 20 examinations that focused on registered investment advisers that engaged in cross trades and/or principal trades involving fixed income securities. The Risk Alert states that nearly two-thirds of the examined advisers received deficiencies, and that "the content and effectiveness of the examined advisers' compliance programs varied greatly."

Exam Priorities – On March 3, 2021, the Division of Examinations announced its 2021 examination priorities.

The annual publication is part of a broader report that includes a summary of the Division's activities in the prior year as well as general statements of Division views on certain topics and broad areas of focus

or concern in the current year (in addition to the more specific stated examination priorities, addressed below). Discussion of these matters included the following:

- The unprecedented challenges presented by and the profound effects of the significant events of 2020, including not only the COVID-19 pandemic, but also the increase in serious cybersecurity incidents and the Division's heightened focus on cybersecurity generally.
- The Division's continued belief in the importance of compliance programs, chief compliance officers, and other compliance staff that play critically important roles at firms, and that culture and tone from the top are key, noting that the hallmarks of effective compliance become apparent in the Division's conduct of examinations.
- The Division believes that there remains significant risk that, in light of industry growth and increased complexity and other factors, it does not have sufficient resources to adequately cover registered investment advisers without staffing increases, creating potential risks of diminished coverage, quality and effectiveness.

Certain areas of focus by the Division in 2021 relevant to hedge fund and private equity fund managers include:

- *Investment adviser compliance programs*. The Division typically assesses compliance programs of registered investment advisers in one or more core areas, including portfolio management practices, custody and safekeeping of client assets, best execution, fees and expenses, business continuity plans and valuation of client assets. In evaluating the effectiveness of a compliance program, the Division frequently reviews whether advisers appear to have sufficient resources to perform core compliance responsibilities. The Division will prioritize examinations of advisers that have not been examined for a number of years. The Division will also continue to conduct examinations of advisers that have never been examined, including new advisers.
- *Registered investment advisers to private funds*. The Division will assess compliance risks, including a focus on liquidity and disclosures of investment risks and conflicts of interest. The Division also will focus on advisers to private funds that have a higher concentration of structured products, such as collateralized loan obligations and mortgage-backed securities (to assess whether the funds are at a higher risk for holding non-performing loans and having loans with higher default risk than that disclosed to investors) as well as advisers to private funds where there may have been material impacts on portfolio companies in which they invest due to recent economic conditions.

Potential Future Rulemakings

On November 10, 2021, in prepared remarks before a meeting sponsored by the Institutional Limited Partners Association, Chairman Gensler presented his views on the role and importance of private equity funds and hedge funds in the U.S. capital markets, and listed five areas in which he has asked the SEC staff to consider recommendations: transparency of fees and expenses, transparency and content of side letters, transparency of performance metrics, contractual waivers of fiduciary duties and conflicts of interest, and potential expansions of the information reported on Form PF. If the staff's consideration of these areas results in proposed rulemakings, it could constitute a significant expansion of the SEC's regulation of private funds and their advisers. Please see our client alert for discussion of Chairman Gensler's speech and what it might mean for developments in this space.

As reflected in the SEC's Regulatory Flexibility Agenda (the "Reg Flex Agenda"), in the spring of 2021, the agency's Division of Investment Management was considering recommending that the SEC propose amendments to existing rules and/or propose new rules under the Advisers Act to improve and modernize the regulations around the custody of funds or investments of clients by investment advisers. The Reg Flex Agenda also includes future rulemaking on ESG issues, and potential amendments to Form PF.

CFTC / NFA Updates

As of the date of writing this review, the CFTC has not yet issued its 2021 annual report on the activities of its Enforcement Division or its annual report on whistleblower activities. However, all indications are that the agency intends to continue to aggressively expand its enforcement capabilities and activities, commencing actions against wrongdoers involving allegations of manipulation, spoofing, fraud, misappropriation of confidential information, and illegally offering new products. On October 21, 2021, for example, the CFTC announced an award of nearly $200 million to a whistleblower who assisted in a CFTC investigation that led to a successful enforcement action.

The NFA examination program appears to be continuing at its normal pace, but with all examinations taking place remotely.

Cryptocurrencies

The CFTC has taken a number of actions reaffirming its intention to play an active role in regulating cryptocurrency markets.

On October 15, 2021, the CFTC issued two significant orders related to cryptocurrencies. The first, against Tether Holdings Limited, Tether Limited, Tether Operations Limited, and Tether International Limited (d/b/a Tether), found that Tether had made untrue or misleading statements in connection with the U.S. dollar tether token (USDT), a stablecoin pegged to the U.S. dollar. The order required Tether to pay a civil monetary penalty of $41 million and to cease and desist from any further violations of the Commodity Exchange Act (CEA) and CFTC regulations.

The order stated that, between June 2016 and February 2019, Tether falsely claimed that its digital tokens were fully backed by fiat currencies. Tether claimed that it had one U.S. dollar in reserves to back every Tether token, but the order found that Tether only held that amount for 27% of the days in the sample period. The CFTC made clear, however, that the agency does not regulate stablecoins and does not have "daily insights in the businesses" surrounding stablecoins.

On the same day, the CFTC issued a separate order filing and settling charges against iFinex Inc., BFXNA Inc., and BFXWW Inc. (d/b/a Bitfinex) in connection with their operation of the Bitfinex cryptocurrency trading platform. The order found that Bitfinex engaged in illegal off-exchange retail commodity transactions in digital assets with U.S. persons on the Bitfinex trading platform and operated as a futures commission merchant (FCM) without registering as required under the CEA and CFTC rules. The order required Bitfinex to pay a $1.5 million civil monetary penalty and required Bitfinex to implement and maintain additional systems reasonably designed to prevent unlawful retail commodity transactions with U.S. customers. It is interesting to note that the CFTC in the order thanked regulatory authorities for their cooperation in the Bahamas, British Virgin Islands, Canada, Panama, Portugal, and the Seychelles.

On September 28, 2021, the CFTC issued an order filing and settling charges against Payward Ventures, Inc. (d/b/a Kraken) for illegally offering margined retail commodity transactions in digital assets, including Bitcoin, and failing to register as an FCM. The order found that from approximately June 2020 to July

2021, Kraken offered margined retail commodity transactions in digital assets to U.S. customers who were not eligible contract participants (ECPs) in violation of U.S. rules. According to the order, Kraken served as the sole margin provider and maintained physical and/or constructive custody of all assets purchased using margin for the duration of a customer's open margined position. The order required Kraken to pay a $1.25 million civil monetary penalty.

In August 10, 2021, the cryptocurrency exchange BitMEX agreed to pay $100 million in civil penalties as part of a settlement with the CFTC and FinCEN. The fine was based upon charges that the exchange allowed illegal trades by U.S. persons in violation of U.S. commodities rules and violated anti-money laundering laws. According to the order, BitMEX did not implement or maintain compliant anti-money laundering programs, failed to report suspicious activity, and deliberately altered customer information to hide customers' true locations. The order states that the exchange's founders established and operated the exchange outside of the United States and accepted funds and orders unlawfully from U.S. customers in violation of U.S. rules, which generally prohibit sales of futures and swap contracts based on commodities (including cryptocurrencies) to U.S. persons unless approved by the CFTC. As a condition of the settlement, BitMEX was required to hire an independent consultant who must analyze future transactions and review BitMEX's compliance policies and procedures.

The conclusion would appear to be that, while the CFTC does not necessarily regulate spot trading for virtual currencies such as Bitcoin and Ether (although CFTC anti-fraud rules would apply), it does intend to regulate any cryptocurrency-related products that involve either a forward or leverage component.

Finally, on October 21, 2021, the CFTC announced that it had filed a civil enforcement action in the Western District of Texas against Abner Alejandro Tinoco, and his company, Kikit & Mess Investments, LLC, both of El Paso, Texas, charging them with fraudulent solicitations and misappropriation of over $3.9 million obtained from at least 61 clients to manage their trading in customized client portfolios for transacting in cryptocurrencies and the foreign exchange markets (forex). The complaint alleges that the defendants misappropriated the funds for Tinoco's personal benefit or to pay false "profits" they reported to clients in a manner similar to a Ponzi scheme. The vast majority of the funds were used to pay Tinoco's personal expenses, such as travel costs, including chartering a private jet, renting a luxury mansion and cars, leasing a luxury automobile, as well as purchasing real estate. On October 13, 2021, U.S. District Court Judge David C. Guaderrama signed an *ex parte* statutory restraining order freezing assets controlled by the defendants, preserving records, and appointing a Temporary Receiver. A hearing on the CFTC's Motion for Preliminary Injunction was scheduled for October 27, 2021. The CFTC seeks restitution to defrauded investors, disgorgement of ill-gotten gains, civil monetary penalties, permanent trading and registration bans, and a permanent injunction against further violations of the CEA, as charged. While the involvement of cryptocurrencies in the action may be viewed as incidental, the case further demonstrates the CFTC's willingness to aggressively investigate and prosecute actions against wrongdoers involving allegations of fraud and misappropriation, including with respect to cryptocurrencies.

CFTC Position Limits

CFTC rules imposing spot-month position limits for 25 physical commodity derivatives became effective on March 15, 2021, with compliance dates of January 1, 2022 for speculative position limits for 16 futures contracts and January 1, 2023 for certain economically equivalent swaps.

NFA Guidance on Branch Offices

In September 2021, consistent with previous NFA guidance permitting employees of NFA member firms (including commodity pool operators ("CPOs") and commodity trading advisors ("CTAs")) to work remotely, the NFA amended the definition of "branch office," which is required to be reported to the NFA, to exclude any location (other than the main business address of the NFA member firm) where one or more associated persons ("APs") from the same household live, provided that: (i) the remote location is not held out to the public as an office of the NFA member firm; (ii) the AP does not meet in-person with customers or physically handle customer funds at the location; and (iii) any CFTC or NFA-required records created at the remote office location are accessible for inspection at the NFA member firm's main or applicable listed branch office as required under CFTC and NFA rules.

NFA Guidance on Supervision of Third-Party Service Providers

In March 2021, the NFA adopted an Interpretive Notice that requires any NFA member that outsources regulatory functions to adopt and implement a supervisory framework over its outsourcing in order to limit any related risks. The NFA indicated that the supervisory framework must address initial risk assessment, onboarding due diligence, ongoing monitoring, termination, and recordkeeping requirements. The Interpretive Notice became effective on September 30, 2021.

Alternative Data

Alternative data, or data garnered from non-traditional sources as described below, is increasingly being used by advisers to private funds and registered investment companies as part of their business and investment decision-making processes.

Alternative data sources offer private fund managers information that cannot be found in traditional company filings, conversations with management, technical analysis or other popular investment factors. Examples of alternative data include, among many other sources: geolocation (*e.g.*, foot traffic), credit card transactions, email receipts, point-of-sale transactions, website usage data, mobile app or app store analytics, satellite images, social media posts, online browsing activity, shipping container receipts, product reviews, price tracking, shipping trackers, internet activity, and quality data.

In response to alternative data's increased popularity with investment advisers, the SEC has honed in on alternative data in response to its use. The SEC's Division of Examination announced in its 2021 Examination Priorities that it will scrutinize whether firms are implementing appropriate controls and compliance around the creation, receipt, and use of information obtained through alternative data sources. 2021 brought to conclusion several alternative data targeted exams of large hedge fund managers with a few deficiency letters being issue. The deficiencies mainly focused on whether the advisers: (i) had policies and procedures tailored to the acquisition and use of alternative data and whether they were being followed; and (ii) followed up on "red flags" that arose during their due diligence of alterntive data providers.

Other noteworthy developments in the alternative data industry are as follows.

SEC Brings First Enforcement Action Against Alternative Data Provider

On September 14th, 2021, the SEC filed a settled securities fraud action against App Annie Inc. and its CEO (collectively "App Annie"), a leading alternative data provider with respect to mobile app

performance data. The settlement is the first enforcement action brought by the SEC against an alternative data provider.

App Annie offered a free app analytics product called "Connect," which enabled companies to visualize and track how their apps were performing. The SEC alleged that App Annie misrepresented in communications with Connect users and through its terms of service that the ways that App Annie could use Connect users' data would be limited. For example, App Annie representatives were trained to respond to inquiries from Connect users that Connect data would be "aggregated" and "anonymized" before being entered into a "statistical model" that generated "estimates."

App Annie's business model relied on selling estimates of how apps belonging to certain companies were performing. App Annie sold these estimates through a paid subscription product called "Intelligence," which included estimates of app revenue, app downloads, and app usage. The SEC alleged that App Annie assured paying subscribers, including many hedge funds, that it had processes and internal controls in place to ensure that it was not selling material non-public information through Intelligence. Specifically, App Annie represented that public company Connect data were not used to generate Intelligence estimates.

However, during most of the relevant period, the SEC alleged that App Annie did not have effective internal controls, and, contrary to representations and other assurances made by App Annie, certain public companies' Connect data had been used to generate Intelligence estimates.

The SEC charged App Annie and its CEO with violations of the antifraud provisions of the Exchange Act. The action highlights that the SEC is focused on alternative data providers, and that it will bring enforcement actions based upon fraud in the alternative data space. It is also likely that they will bring actions under Section 204A of the Advisers Act alleging that investment advisers failed to establish, maintain and enforce written policies and procedures reasonably designed to prevent the misuse of material, non-public information in connection with the acquisition and use of alternative data. While the SEC did not allege that either App Annie or its CEO were purchasers or sellers of securities, the SEC apparently relied on a broad reading of the "in connection with" language in the antifraud statue and rule. For additional information please see our client alert.

Supreme Court Vacates LinkedIn-hiQ Labs Scraping Decision, Remands to Ninth Circuit for Another Look

On June 14, 2021, the Supreme Court vacated and remanded the Ninth Circuit's 2019 ruling in *LinkedIn Corp. v. hiQ Labs, Inc.*, which held that hiQ Labs, Inc. ("hiQ") did not violate the Computer Fraud and Abuse Act ("CFAA") by data scraping public profiles on LinkedIn Corp.'s ("LinkedIn") website. The case was sent back to the Ninth Circuit for further consideration in light of the Supreme Court's holding in *Van Buren v. United States*, which narrowed the interpretation of "exceeds unauthorized access" under the CFAA. For more information see our blog post.

LinkedIn Corp. v. hiQ Labs, Inc.

HiQ used automated bots to capture information from public profiles on LinkedIn in order to generate "people analytics," which it sold to its clients. In response, LinkedIn took steps to prohibit such behavior, including signaling to automated bots that they are prohibited from accessing LinkedIn servers, blocking automated attempts to scrape data and sending hiQ a cease-and-desist letter. LinkedIn asserted in a claim against hiQ that hiQ violated the CFAA, which prohibits "accessing a computer without authorization or exceeding authorized access." When the case reached the Ninth Circuit, the court ruled against

LinkedIn and held "it is likely that when a computer network generally permits public access to its data, a user's accessing that publicly available data will not constitute access without authorization under the CFAA."

Van Buren v. United States

In *Van Buren v. United States*, a former police sergeant was charged with violating the CFAA for using his computer to access a government database and retrieve information about a particular license plate. The Supreme Court held that this behavior did not violate the CFAA because "exceed[ing] authorized access" under the CFAA only prohibits unauthorized access, not "unauthorized uses." In its decision the Supreme Court adopted a "gates up or down" approach to interpreting the CFAA, meaning one either can or cannot access a computer system or certain areas within such computer system.

Impact of Van Buren on hiQ

Unlike in *Van Buren*, the CFAA "without authorization" issue is more nuanced in the *hiQ* scraping context. In *Van Buren* the police sergeant had the requisite authority to access the computer he used. Conversely, in *hiQ*, it is ambiguous whether hiQ lost authority to use publicly accessible information once LinkedIn took preventative measures. On remand, *hiQ* will likely hinge on whether technical measures to block access to LinkedIn's site followed by a formal revocation of access truly lowers the access gate (for purposes of CFAA liability), or whether the gate for public website content is always up and no CFAA liability may arise for such access to publicly available website data. The Ninth Circuit will be asked again to decide whether the CFAA's "without authorization" provision is limited to computer information for which access permission, such as password authentication, is generally required. Importantly, the Supreme Court declined to decide in *Van Buren* whether authorized access turns on only code-based restrictions (such as a password to access a computer).

Settlement in Plaid Fintech Data Case

On August 5, 2021, a proposed class action settlement was reached in the suit against startup financial technology ("fintech") services company, Plaid Inc. ("Plaid"). Plaid provides account linking and verification services for fintech apps that consumers use to send and receive money from their bank accounts.

In a civil class action law suit filed against Plaid, the plaintiffs argued that Plaid violated their privacy by obtaining their financial account information without their consent. Fintech apps typically verify a user's bank account by redirecting the user to the bank's platform where they are prompted to log in. The bank in turn allows the app to access the necessary information without giving it access to the user's login information. Plaid, however, designed its login screens to mimic the look and feel of the login screens of individual financial institutions. Plaintiffs allege that users were not informed that they were not logging into their bank's own platform, and that they unwittingly gave Plaid their login credentials. They claim that Plaid retained access to their credentials and used them to mine, aggregate, and sell users' financial transaction data to third parties. At no time, according to the plaintiffs, were users given conspicuous notice or meaningfully prompted to read through the privacy policy indicating that Plaid was taking such actions.

In the proposed settlement, Plaid has agreed to change privacy and data collection practices, delete certain data it collected, and provide a $58 million fund for the settlement class of consumers. This action is one of the increasing number of actions being filed concerning mobile data collection practices, as the collection and use of consumer data has become more highly scrutinized in recent years.

For more information see our blog post.

Mobile Platforms Block Data Broker from Collecting User Location Data

In December 2020, the *Wall Street Journal* reported that Apple and Google told app developers to remove the X-Mode Social Inc. ("X-Mode") social tracking software development kit ("SDK") from their apps or face being removed from the platforms' app stores. The decision by Apple and Google was announced following reports that X-Mode was selling location data to government entities and defense contractors. X-Mode pays developers to include its SDK in their apps in exchange for providing users' location data. Google has since also requested that developers remove code from another location data broker, Predicio, which has been connected to a government contractor that has sold location data to government agencies.

The sale of location data has come under greater scrutiny as privacy laws become more stringent and public awareness of locational data sharing grows. In the past year, a group of Senators, including Senator Ron Wyden of Oregon, have solicited government inquiries into the sale of location data to government agencies and contractors. Senator Wyden argues that commercial data brokers' sale of location data to government entities is unlawful without a warrant, citing Supreme Court decision *Carpenter v. United States*, which held that the acquisition of cell-site location information constitutes a Fourth Amendment search.

The question arises of whether Apple and Google's actions signal the beginning of the end of widespread location sharing on mobile phones, or of the sharing of locational data with government entities. Given the heightened scrutiny of the sharing of user data, recipients of aggregated user data should take care to perform due diligence and understand how the data was collected and whether such collection comports with contractual and mobile platform requirements.

Insider Trading Update

The past 12 months saw two significant decisions from the U.S. Court of Appeals for the Second Circuit: one addressing insider trading in breach of a confidentiality agreement, and another holding that the existence of a fiduciary duty is not necessary for securities fraud based on deceptive trading, rather than on "insider trading." Other noteworthy events included (i) the vacatur and remand of another Second Circuit decision allowing the government to pursue criminal insider-trading cases based on 18 U.S.C. § 1348, instead of on the more traditional securities-law provisions, (ii) an SEC enforcement action based on "shadow trading," (iii) the CFTC's continued interest in insider trading, and (iv) Congressional bills addressing trading-related issues.

New Decisions from the Second Circuit on Duties and Personal Benefits

The Second Circuit issued two decisions in the past year concerning the types of conduct and duties that can give rise to liability for securities fraud.

In April 2021, the Second Circuit affirmed the insider-trading conviction of the principal of a potential acquiror who, in breach of a non-disclosure agreement with a potential target company, had provided a tippee with non-public information about an impending acquisition of the target. The decision in *United States v. Chow*, 993 F.3d 125 (2d Cir. 2021), held that:

- The non-disclosure agreement ("NDA") between the transaction parties created a duty to keep information about the potential transaction confidential and not to use it for any purpose other than the transaction;
- The defendant tipper violated the NDA by providing information to the tippee, who purchased significant amounts of the target's shares before the transaction was announced;
- The evidence supported the jury's finding that the tipper had intentionally provided material, non-public information ("MNPI") to the tippee; and
- The tipper had received a sufficient personal benefit in exchange for providing MNPI.

In July 2021, the Second Circuit affirmed the securities fraud conviction of traders who had traded on information from stolen, pre-publication press releases. The decision in *United States v. Khalupsky*, 5 F.4th 279 (2d Cir. 2021), held that:

- The existence of a fiduciary duty is not necessary to establish fraudulent trading by an outsider;
- The use of stolen credentials to gain access to information-technology systems is deceptive conduct within the meaning of the securities laws; and
- Conscious avoidance suffices to establish the state of mind necessary for criminal liability for securities fraud.

United States v. Chow

The *Chow* case involved the attempted acquisition of a U.S. semiconductor manufacturer by an entity allegedly affiliated with the Chinese government. At several points during the acquisition effort, the tipper (Chow) – on behalf of the potential acquiror – and the target had signed NDAs providing that the parties would not disclose or use any proprietary information of the other party except for purposes of the potential transaction and that "[t]he fact of the exploration and evaluation of a potential strategic transaction" was itself confidential. The parties also had taken other precautions to keep their negotiations confidential.

During the negotiation process, the tipper allegedly communicated multiple times with the tippee and supposedly provided information about the negotiations. The communications allegedly occurred close to significant points in the transaction process, including the making of offers and the exchange of a draft merger agreement. The tippee bought large amounts of the target's shares for multiple accounts shortly after those communications. The tippee then sold about half of those shares on the day the transaction was announced. (The deal ultimately was blocked by the Committee on Foreign Investment in the United States ("CFIUS").)

The tipper was prosecuted for insider trading under § 10(b) of the Exchange Act, securities fraud under 18 U.S.C. § 1348, and conspiracy to commit securities fraud. The jury convicted the tipper on some (but not all) of the insider-trading counts relating to the tippee's purchases and on the securities-fraud and conspiracy counts.

The tipper appealed, arguing that the NDA had not created a duty of confidentiality, the evidence had not established an intentional breach of the NDA, and the tipper had not sought or received a personal benefit. The Second Circuit affirmed the conviction.

The Second Circuit first held that (i) the NDA imposed a legal duty of confidentiality on the tipper, (ii) the tipper breached that duty by allegedly disclosing information about the transaction, and (iii) this breach of duty created liability under the misappropriation theory of insider trading. The court noted that SEC Rule 10b5-2 expressly addresses this situation, stating that, "[w]henever a person agrees to maintain information in confidence,… a duty of trust or confidence exists."

The court also held that the jury had received sufficient evidence to conclude that the tipper had intentionally disclosed MNPI to the tippee. The two had known each other for at least five years; the tipper had "a strong interest in being able to communicate with" the tippee; the tipper's phone had five numbers stored for the tippee; and the tipper had revealed more than "his own thoughts" about the progress of the merger negotiations.

Perhaps most interesting was the Second Circuit's treatment of the "personal-benefit" requirement – the requirement that a tipper receive some type of personal benefit in exchange for providing MNPI to a tippee. The court reiterated its prior ruling that "the government need not show that the tipper expected or received a specific or tangible benefit in exchange for the tip, and that the personal benefit element is satisfied where there is evidence that the tipper intend[ed] to benefit the . . . recipient."

The court first recited specific types of benefits that the tipper allegedly had received: the tipper had asked the tippee to provide him with analyst reports on the semiconductor industry and to recommend possible limited partners for the tipper's business venture; the tippee had given the tipper information about other manufacturers and users of the target's main product; the tippee had used his contacts with investment bankers to connect the tipper with an analyst knowledgeable about the target's product; and the tippee had sent the tipper gifts of wine and cigars.

But the court seemed to focus more on the other aspect of the personal-benefit requirement, which finds a sufficient personal benefit where the tipper simply intends to benefit the tippee even without receiving anything specific in return. The court found the record sufficient to support inferences that the tipper had "knowingly and intentionally breached his duty of confidentiality by disclosing material nonpublic information as to the prospects for a merger agreement between [the target] and [the tipper's] fund, intending for [the tippee] to make trades based on that information."

The *Chow* decision does not break new ground on any of the issues it addressed. In fact, the court's discussion of the NDA and the legal duty it created relied heavily on the court's decision in *United States v. Kosinski*, 976 F.3d 135 (2d Cir. 2020), which we addressed in our insider-trading update last year. The personal-benefit discussion, although not novel, reinforces that such a benefit can exist even where the tipper does not receive something in exchange for the tip. An intent to benefit the tippee and enable him or her to trade on MNPI can suffice.

United States v. Khalupsky

The *Khalupsky* case involved two defendants – a hedge-fund manager and investment adviser, and the owner of a trading company – who had traded on non-public information stolen by hackers in Ukraine from three newswires. The hackers had obtained not-yet-published press releases containing material financial information and had saved the press releases on a web-based server, to which the defendants were given access. The defendants were convicted of securities fraud and conspiracy to commit wire fraud and securities fraud. The Second Circuit affirmed the convictions.

The Second Circuit first rejected the defendants' argument that they could not be liable for securities fraud because they had not owed a fiduciary duty to investors of the companies whose press releases

had been stolen and because any deception employed in obtaining the press releases had not targeted the investors. The court held that, "although a fiduciary duty is relevant to other securities violations – *e.g.*, insider trading – it need not be shown to prove the securities fraud charged here: fraudulent trading in securities by an outsider." The court also held that the argument that the deception must have targeted investors "contradicts the plain language of Rule 10b-5," which requires only that deception be "'*in connection with* the purchase or sale of any security," as it was in this case.

The court next held that the hack of the newswires' systems qualified as a "deceptive device or contrivance" under § 10(b). The hackers had extracted employees' log-in credentials and used them "to intrude into the system's more secure areas." The use of "stolen employee login credentials to gain further system access was deceptive" because, "every time the hackers attempted to access parts of the system by entering stolen credentials, they misrepresented themselves to be authorized users." Misrepresentation of one's identity to gain access to otherwise off-limits areas, and then stealing the information in those areas, is "deceptive" under the securities laws. This ruling tracked the Second Circuit's decision in an earlier case involving another Ukrainian hacker, *SEC v. Dorozhko*, 574 F.3d 42 (2d Cir. 2009).

The court also ruled that the jury charge's "conscious avoidance" instruction could satisfy the knowledge requirement for securities fraud. The District Court had charged the jury:

> To determine whether the defendant acted knowingly[,] you may consider whether the defendant deliberately closed his eyes as to what would otherwise have been obvious to him. If you find beyond a reasonable doubt that the defendant acted or that the defendant's ignorance was solely and entirely the result of a conscious purpose to avoid learning the truth, then this [knowledge] element may be satisfied.

The Second Circuit concluded that the charge was legally correct and that the jury could reasonably have inferred that the defendants had been "aware of a high probability of the fact in dispute and consciously avoided confirming that fact. . . . The jury would have been entitled to infer that the need for password-protection signaled to [the defendant] that the press releases – documents usually publicly disseminated without the need for security – had been illicitly obtained, and that he chose not to confirm that suspicion."

Securities Fraud Liability Without Personal Benefits and Fiduciary Breaches?

Our annual updates over the past several years have examined the evolution of the "personal benefit" requirement from the Second Circuit's decision in *United States v. Newman*, 773 F.3d 438 (2d Cir. 2014), through the Supreme Court's decision in *Salman v. United States*, 137 S. Ct. 420 (2016), and the Second Circuit's rulings in *United States v. Martoma*, 894 F.3d 64 (2d Cir. 2018). The debate centered on the nature of the "personal benefit" that a tipper of MNPI must obtain to create tipper and tippee liability for trading based on that information.

Insider-trading liability arises under § 10(b) of the Exchange Act only if securities were bought or sold on the basis of MNPI used or obtained in breach of a fiduciary duty or a duty of trust or confidence owed to the shareholders of the issuer or to the source of the information. That breach of duty depends on whether the tipper received a personal benefit in exchange for providing the information.

However, as we previously discussed, a criminal fraud statute enacted as part of the Sarbanes-Oxley Act of 2002 – 18 U.S.C. § 1348 – does not facially require consideration of either fiduciary breaches or personal benefits, and its intent requirement differs from § 10(b)'s. Section 1348 imposes criminal liability on anyone who "knowingly executes, or attempts to execute, a scheme or artifice" either (1) "to defraud

any person in connection with" any commodity or any security of a registered issuer or (2) "to obtain, by means of false or fraudulent pretenses, representations, or promises, any money or property in connection with the purchase or sale" of any such commodity or security.

Accordingly, prosecutors have been using § 1348 in insider-trading cases, and the Second Circuit's December 2019 decision in *United States v. Blaszczak*, 947 F.3d 19 (2d Cir. 2019), *judgment vacated*, 141 S. Ct. 1040 (2021), seemed to confirm the availability of that alternative theory of criminal liability. But reliance on § 1348 and *Blaszczak* might have hit a speed bump – if not a potential roadblock in some cases—when the Supreme Court vacated the judgment and remanded for further consideration in light of the Court's decision in the "Bridgegate" case, *United States v. Kelly*, 140 S. Ct. 1565 (2020).

The Blaszczak Case

Blaszczak, as our readers might recall, involved prosecutions of four individuals in connection with alleged schemes to obtain non-public information from the federal Centers for Medicare and Medicaid Services (the "CMS") about reimbursement rates for certain medical treatments. A CMS employee had allegedly given MNPI to a friend (Blaszczak), a former CMS employee who was then working as a consultant; the consultant then passed the information to persons at two hedge funds, who traded on it. The CMS employee allegedly had received benefits from the tippee-consultant in the form of free meals, tickets to sporting events, and an offer to join the consultant's firm.

The government charged all defendants with securities fraud under § 10(b) and also with violations of § 1348 and the wire-fraud and conversion statutes. The court's jury instructions on the § 10(b) charge addressed the standard elements – including whether the tipper (the CMS employee) had owed and breached any duty of trust or confidence to his agency, whether he had received a personal benefit for doing so, and whether the tippee defendants had known of the tipper's breach of duty and receipt of a benefit. The defendants asked the court to include those same elements in its charge under § 1348, but the court denied the request, requiring the jury to find only that the defendants had knowingly and willfully engaged in "an illegal scheme or artifice" by providing confidential CMS information "to another person for the purpose of buying or selling securities on the basis of that information." The charge did not say anything about the tipper's duty to the agency, his alleged receipt of a personal benefit, or the tippees' knowledge of either of those things.

The jury acquitted the defendants on the § 10(b) charges, but convicted them of § 1348 violations (except the CMS employee, who was convicted of wire fraud and conversion of government property).

The Second Circuit, in a 2-1 decision, affirmed the convictions, holding that the personal-benefit test required for Title 15 securities fraud under § 10(b) does not apply to Title 18 securities fraud under § 1348 – or to wire fraud under 18 U.S.C. § 1343. The court rejected the defendants' argument that eliminating the personal-benefit requirement from Title 18 securities fraud (and wire fraud) would give the government "a different – and broader – enforcement mechanism to address securities fraud than what had previously been provided in the Title 15 fraud provisions." The court concluded that § 1348 was designed to achieve that result.

The court also held that, "in general, confidential government information may constitute government 'property' for purposes of the Title 18 securities-fraud and wire-fraud statutes. "[G]overnment agencies have strong interests – both regulatory and economic – in controlling whether, when, and how to disclose confidential information relating to their contemplated rules" (here, CMS's rules about reimbursement rates). In addition, the court upheld the convictions under the statute prohibiting conversion of federal

property (18 U.S.C. § 641), ruling that the government's confidential information constituted a "thing of value."

Judge Kearse dissented because she did not consider the agency's pre-decisional regulatory information to be "property" or a "thing of value" under Title 18.

Bridgegate

While *Blaszczak* was making its way through the courts, the seemingly unrelated *Kelly* case arising from Bridgegate was also proceeding. Bridgegate involved alleged political retaliation by the Governor of New Jersey's Deputy Chief of Staff and the Deputy Executive Director of the Port Authority of New York and New Jersey (whom the Governor had appointed) against a local mayor who allegedly had thwarted the Governor's wishes. According to the government's allegations, the Governor – a Republican – was up for reelection and wanted to win a large bipartisan victory to promote his presidential aspirations. The Deputy Chief of Staff sought endorsements from Democratic mayors, including the Mayor of Fort Lee, but the Mayor declined to endorse the Governor. Supposedly in retaliation for the Mayor's refusal to cooperate, the Deputy Chief of Staff worked with the Port Authority's Deputy Executive Director and others to fabricate a "traffic study" that involved closing critical Fort Lee access lanes on the George Washington Bridge, thereby causing traffic to back up and create chaos in Fort Lee.

The government prosecuted the Deputy Chief of Staff and the Port Authority's Deputy Executive Director on charges of wire fraud, fraud on a federally funded program or entity (the Port Authority), and conspiracy to commit those two crimes. The jury found the defendants guilty on all counts, and the Court of Appeals for the Third Circuit affirmed.

The Supreme Court unanimously reversed the convictions in May 2020. The Court held that the statutes at issue prohibited deceptive conduct to deprive the victim of "money or property," so the government needed to prove not only that the defendants had engaged in deception, but also that *property* had been an object of their deception. The realignment of the bridge's traffic lanes, however, was "a quintessential exercise of regulatory power," rather than an appropriation of the Port Authority's property. And while the scheme required the use of a public employee's paid time (which could be considered governmental property), the defendants "never had that as an object.… The use of Port Authority employees was incidental to – the mere cost of implementing – the sought-after regulation of the Bridge's toll lanes," rather than an effort to deprive the government of its property.

Blaszczak Redux

The *Kelly* decision gave new life to an issue that the *Blaszczak* defendants had raised and on which Judge Kearse had based her dissent: whether CMS's confidential, pre-decisional regulatory information was "property" under 18 U.S.C. § 1348 and the wire-fraud statute. Accordingly, the Supreme Court vacated and remanded the *Blaszczak* convictions for further consideration in light of *Kelly*. 141 S. Ct. 1040 (2021).

The Second Circuit heard argument in June 2021, and its decision is pending. Stay tuned for the ruling, which might or might not address the personal-benefit requirement. The Second Circuit might focus only on the "property" issue that *Kelly* raised.

Kelly's "property" analysis would seem to be more relevant when the confidential information at issue comes from a governmental agency (as it did in *Blaszczak*) than when it comes from a corporation or other non-governmental entity. In light of *Kelly*, a governmental entity would seem less justified in considering its confidential information to be "property" than would a non-governmental entity. The

Second Circuit's upcoming decision thus might not affect the viability of using § 1348 in insider-trading cases involving non-governmental entities' MNPI.

Meanwhile, another court recently followed the Second Circuit's vacated *Blaszczak* decision and held that § 10(b)'s personal-benefit test is not an element of a claim for criminal liability under § 1348. *United States v. Ramsey*, 2021 WL 4554631 (E.D. Pa. Oct. 4, 2021). The court agreed with the Second Circuit's construction of § 1348 as well as with its policy conclusion that Congress had intended to make proof of securities fraud under Title 18 less demanding than under Title 15. The court also saw no reason to speculate as to whether the Supreme Court had considered *Blaszczack*'s personal-benefit ruling, as opposed to only the money/property ruling, when the Court vacated and remanded the case for further consideration in light of *Kelly* (which had not involved personal-benefit issues at all).

SEC "Shadow Trading" Action and Potential Complications for Compliance Programs

On August 17, 2021, the SEC charged a former employee of a biopharmaceutical company with insider trading in advance of an acquisition, but with a unique twist: the former employee was trading stock of a company unrelated to the merger. *SEC v. Panuwat*, No. 3:21-cv-6322 (N.D. Cal.).

The former employee, Matthew Panuwat, had not traded his own company's or the acquiring company's securities, but instead had purchased stock options for shares of a competitor not involved in the acquisition, in the belief (as alleged by the SEC) that the competitor's stock price would also benefit from the news. The SEC did not claim that Panuwat had received any particular information from the company whose stock he traded. Instead, the SEC charged that Panuwat had engaged in "shadow trading" of a comparable company by misappropriating information from his employer about the employer's own transaction prospects.

The defendant is litigating the case and challenging the shadow-trading theory, which has not to our knowledge previously been used in an SEC insider-trading case. While the SEC's complaint does not appear to break new ground on the misappropriation theory, it does involve materiality issues that could raise issues for fund managers, particularly in the context of designing compliance programs and evaluating the scope of internal trading restrictions.

Factual Background

Panuwat, who was the then-head of business development at Medivation, was closely engaged in internal discussions in the lead-up to a large pharmaceutical company's acquisition of Medivation, including discussions with and presentations from Medivation's investment bankers. The information that Panuwat learned about Medivation's potential acquisition was non-public, and, under Medivation's insider-trading policies (which he had signed), he had a duty to keep it confidential and not trade securities based on it. However, shortly after learning that Medivation would be acquired at a significant premium, Panuwat purchased call options in Incyte, a competitor of Medivation that was one of the only other oncology-focused mid-cap biopharmaceutical companies remaining as a potential market acquisition target.

The SEC alleged that Panuwat had reason to believe that the announcement of Medivation's acquisition would positively affect Incyte's stock price as well as Medivation's. Indeed, after the Medivation acquisition was announced, Incyte's stock price rose approximately 8%, leading to profits of over $100,000 for Panuwat. The SEC charged Panuwat with insider trading in Incyte securities under § 10(b) of the Exchange Act and Rule 10b-5, based on a misappropriation theory.

Unhelpful Facts for the Defendant

Although the theory of misappropriating information to use in shadow trading of other companies' securities has not yet been tested in court, this case would seem to present a potentially favorable set of facts for the SEC based on the following:

- The defendant had received confidential presentations from Medivation's investment bankers that had specifically drawn parallels between Medivation and Incyte as comparable potential acquisition targets.
- The defendant had reason to believe that the pending acquisition of his company was likely to have a positive impact on Incyte's stock price.
- The defendant purchased out-of-the-money, short-term call options for Incyte shares.
- Information about a pending merger is typically viewed as highly important information (*i.e.*, clearly material).
- Incyte's stock price rose approximately 8% after the Medivation acquisition was announced.
- The defendant had years of experience as an investment banker and in the securities industry generally, had specialized in deals involving the pharmaceutical industry, and had worked closely with Medivation's investment bankers and other high-level Medivation executives to explore Medivation's alternatives, including a possible merger with another company. He previously had held securities licenses and had been associated with a broker-dealer investment bank.
- The defendant had agreed, at the outset of his employment with Medivation, to keep information he learned during his employment confidential and not use it except for the benefit of Medivation. In addition, Medivation's insider-trading policy, which the defendant had signed, expressly addressed trading in other companies' securities and prohibited employees from using confidential information concerning Medivation to trade Medivation securities or "the securities of another publicly traded company, including all significant collaborators, customers, suppliers, or competitors."

Implications

The defendant is challenging the SEC's misappropriation theory on materiality grounds and on whether he breached a duty of trust and confidence. In a motion to dismiss filed on November 1, 2021, Panuwat argued that the SEC "has never before attempted to bring an insider trading case against an individual based solely on the purchase of securities of a company about which neither he nor his employer possessed *any material nonpublic information*," or "against an individual alleging that the individual's duty of trust and confidence to his employer prohibited trading in the securities of an unrelated company operating within the same broadly-defined industry."

However, the facts alleged by the SEC seem to fit within the traditional contours of the misappropriation theory and suggest that the defendant breached a duty to his own employer. The defendant had agreed to keep information he learned during his employment confidential and not to use such information except for his employer's benefit. In addition, as an employee, the defendant presumably owed a duty of confidentiality to his employer and a duty to refrain from using for his personal benefit any non-public information that he received through his employment. He also was subject to an insider-trading policy that appears to have covered the trading at issue: it prohibited trading "the securities of another publicly

traded company, *including* all significant collaborators, customers, suppliers, or competitors" (emphasis added). Panuwat contends that the SEC's complaint does not allege that Incyte was a significant collaborator, customer, supplier, or competitor of Medivation, but the insider-trading policy's use of the word "including" might cut against such a limited reading of the prohibition on trading "the securities of another publicly traded company."

The key question in the case is likely to be materiality, and whether a reasonable investor would have considered the news about Medivation's merger material with respect to Incyte. In the Medivation case, this hurdle might be easier for the SEC to overcome because the investment bankers' materials had specifically listed Incyte as a comparable company. But what if the bankers had not drawn an express comparison between Medivation and Incyte? What if the defendant had figured out the comparison on his own – as might happen in other situations of "shadow trading"?

For fund managers, "shadow-trading" risks can raise issues in terms of enforcing policies and procedures to prevent insider trading. For firms that allow employees "over the wall" to analyze potential transactions on a regular basis, determining which companies should be placed on the firm's restricted list might be more difficult where the information available to the "over the wall" employee does not relate to a specifically identifiable company (such as a party to the transaction at issue) or even to only a small number of identifiable companies. Typically, if MNPI relates to a particular company, a person cannot use that information to trade in major suppliers or customers of that company (that limitation was the apparent focus of Medivation's insider-trading policy). But, taken to its logical conclusion, the SEC's shadow-trading theory could potentially implicate trading in an entire industry based on MNPI relating to only one company, especially in light of SEC Rule 10b5-1's warning that mere awareness of MNPI can constitute trading "on the basis of" MNPI.

For example, confidential information about one company might bolster an analyst's confidence about a broader industry, but is the trader then "aware" of MNPI about the whole industry? The answer might depend on the size and depth of the industry. If the industry involves many similarly situated companies, the non-public information might not be considered too material. But if, as here, the industry allegedly consists of only a handful of similarly situated companies (Incyte supposedly was one of the few oncology-focused mid-cap biopharmaceutical companies remaining as a potential acquisition target), the non-public information might be more likely to be material.

Legal and compliance professionals should think about how far to extend trading restrictions when signing an NDA with a particular company. They should be aware that the restrictions might go beyond the companies at issue and their major suppliers and customers; they might cover a wider swath – such as "the securities of another publicly traded company," as in the *Panuwat* case. In those situations, investment professionals might need to keep an eye out for other companies mentioned in materials contained in a data room, or companies – or perhaps even competitors – that one would reasonably believe might be affected by the particular transaction.

Legal and compliance professionals often hope to avoid having to make trading decisions based solely on assessments of materiality, because those assessments are highly fact-specific and therefore unpredictable from a legal point of view. But at the end of the day, if confidential information about a particular company has potentially broader impact on an entire industry, trading decisions might require assessing the risk that particular information could be material.

CFTC's Continued Interest in Insider Trading

Our previous updates discussed the Commodity Futures Trading Commission's (CFTC) renewed interest in combatting insider trading. That interest continued during the past year, and it included the CFTC's collaboration with the Department of Justice to investigate matters relating to the commodities markets.

On December 3, 2020, the CFTC announced a settlement with Vitol Inc., a commodities trading company, for alleged violations of the Commodity Exchange Act (CEA) arising from a foreign bribery scheme. In addition to alleging that Vitol had bribed foreign government officials, the CFTC's settlement order asserted that the bribes had enabled Vitol to obtain "specific price information" as well as confidential information about a state-owned entity's "projected supply, demand, and strategic planning," and that Vitol employers had traded on that MNPI in the oil markets. The CFTC proceeded on a misappropriation theory, contending that the state-owned entities' employees had breached their duty to their employer to keep that information confidential.

The CFTC's order might be read as taking a broader approach to insider trading than the CFTC took in earlier matters. Instead of alleging that Vitol's traders had traded "on the basis of" MNPI, the order claimed that the traders had traded "while in possession of" MNPI. The CFTC thus might be aligning itself with the SEC's position in Rule 10b5-1(b), which defines trading "on the basis of" MNPI to mean "the person making the purchase or sale was *aware of* the [MNPI] when the person made the purchase or sale" (emphasis added).

Legislation on Insider Trading: Again, Not Much Progress

As we previously reported, several bills were introduced in Congress in recent years to address insider trading. None of them became law because of lack of progress in the Senate. The same has been true of the past 12 months.

The House's "Insider Trading Prohibition Act"

On May 18, 2021, the House passed H.R. 2655, the "Insider Trading Prohibition Act," which would prohibit the purchase or sale of securities while the trader is "aware of [MNPI] relating to such security," or "any nonpublic information, from whatever source, that has, or would reasonably be expected to have, a material effect on the market price of any such security," if the trader "knows, or recklessly disregards, that such information has been obtained wrongfully, or that such purchase or sale would constitute a wrongful use of such information." The bill also prohibits any such person from "wrongfully" communicating MNPI if (i) the person who receives the communication purchases or sells the security at issue or communicates the MNPI to someone else who does so and (ii) "such a purchase or sale . . . while aware of such information is reasonably foreseeable."

Trading while aware of MNPI, or communicating MNPI, would be "wrongful" "only if the information has been obtained by, or its communication or use would constitute, directly or indirectly,"

- "Theft, bribery, misrepresentation, or espionage (through electronic or other means)";
- "A violation of any Federal law protecting computer data or the intellectual property or privacy of computer users";
- "Conversion, misappropriation, or other unauthorized and deceptive taking of such information" or

- A breach of any fiduciary duty, confidentiality agreement, contract, code of conduct or ethics policy, or "any other personal or other relationship of trust and confidence for a direct or indirect personal benefit (including pecuniary gain, reputational benefit, or a gift of confidential information to a trading relative or friend)."

The person trading while aware of MNPI, or communicating MNPI, need not know "the specific means by which the information was obtained or communicated, or whether any personal benefit was paid or promised by or to any person in the chain of communication, so long as the person trading while aware of such information or making the communication . . . was aware, consciously avoided being aware, or recklessly disregarded that such information was wrongfully obtained, improperly used, or wrongfully communicated."

The bill thus would appear to codify aspects of insider-trading law as we know it, including the relatively expansive definition of "personal benefit" and the SEC's position in Rule 10b5-1 that a person trades "on the basis of" MNPI if he or she was "aware of" it. However, unlike current insider-trading law, the bill does *not* appear to require that the person trading on or disclosing MNPI had known whether a personal benefit had been paid or promised. On the contrary, the bill says that the knowledge component does *not* require the trader to know "the specific means by which the information was obtained or communicated, or whether any personal benefit was paid or promised by or to any person in the chain of communication, so long as the person trading while aware of such information . . . was aware, consciously avoided being aware, or recklessly disregarded that such information was wrongfully obtained, improperly used, or wrongfully communicated."

The bill further states that, except as provided in Exchange Act § 20(a), a controlling person shall not be liable "solely by reason of the fact that such person controls or employs a person who has violated this section, if such controlling person or employer did not participate in, or directly or indirectly induce the acts constituting a violation of this section." This provision could provide protection to a fund whose employee has gone rogue, as long as the fund itself did not profit from or directly or indirectly induce the alleged misconduct.

The bill also carves out transactions made pursuant to trading plans under SEC Rule 10b5-1. In addition, the bill directs the SEC to review Rule 10b5-1 and make any necessary modifications.

The Senate has not acted on the bill.

Senate Bills Requiring SEC Studies

Two bills have been introduced – but not passed – in the Senate requiring the SEC to conduct studies and promulgate or amend rules relating to insider trading.

S. 2211, the "Promoting Transparent Standards for Corporate Insiders Act," was introduced in June 2021. This bill would require the SEC to conduct a study to determine whether Rule 10b5-1 (concerning insiders' trading plans) should be amended to:

- Limit issuers' and insiders' adoption of trading plans to issuer-adopted trading windows;
- Limit issuers' and insiders' ability to adopt multiple trading plans;
- Establish a mandatory delay between the adoption of a trading plan and the execution of the first trade;
- Require issuers and insiders to file trading plans; and

- Require Boards of Directors to adopt policies concerning trading plans.

The SEC's study would be due within 180 days after enactment of the legislation, and the SEC would be required to amend Rule 10b5-1 within one year after enactment.

S. 2360, the "8-K Trading Gap Act of 2021," was introduced in July 2021. This bill would require the SEC, within one year after the proposed legislation's enactment, to issue rules requiring issuers to establish policies, controls, and procedures to prevent executive officers and directors from trading the issuers' securities between (i) either the date a reportable event occurs (for Form 8-K §§ 1-6) or the date the issuer determines to report that event (for Form 8-K §§ 7-8) and (ii) the date the issuer files a Form 8-K or furnishes it to the SEC. The SEC may exempt "automatic" transactions, such as those made pursuant to advance election or trading plans, but not if the trading plans were adopted during the pre-8-K periods described in the preceding sentence.

Private Fund Litigation

This has been a relatively quiet year for significant commercial litigation cases involving private funds. However, in one notable decision, *AmerisourceBergen Corp. v. Lebanon County Employees' Retirement Fund*, the Delaware Supreme Court affirmed a Chancery Court's decision adopting an expansive view in favor of parties seeking information from companies under Section 220 of the Delaware General Corporation Law.

Section 220 allows stockholders to inspect books and records of a Delaware corporation for any proper purpose and to compel inspection if refused. Recognized "proper purposes" to inspect books and records include, among others, determining director independence and investigating disclosures, waste, and possible mismanagement or self-dealing. For investigatory purposes, stockholders must demonstrate a credible basis to infer possible mismanagement warranting further investigation, a standard Delaware courts have described as the lowest possible burden of proof. Section 305 of the Delaware Limited Partnership Act and Section 305 of the Delaware Limited Liability Company Act ("Delaware LLC Act") provide comparable remedies for limited partners and LLC members, respectively.

In affirming the Chancery Court's order, the Court acknowledged that while "a mere statement of suspicion" would be inadequate, where a stockholder "present[s] a credible basis from which the court can infer wrongdoing or mismanagement," it has met its burden of identifying a proper investigatory purpose. The Court also rejected the company's contention that stockholders were required to demonstrate that the alleged wrongdoing they sought to investigate was legally actionable, finding that any such actionability requirement would be at odds with the "credible basis" standard for investigative inspections under Section 220, and would detract from the intended summary nature of Section 220 proceedings. Finally, the Court concluded that the Chancery Court did not abuse its discretion by, on its own initiative, permitting the plaintiffs to conduct a deposition "to explore what types of books and records exist and who has them."

The *AmerisourceBergen* decision sheds further light on what constitutes a proper investigative purpose under Section 220 – as well as under Section 305 of the Delaware Limited Partnership Act and Section 305 of the Delaware LLC Act. Though the opinion acknowledges that companies can still challenge the veracity of stockholders' articulated investigative purposes, it also encourages plaintiff stockholders (and by extension limited partners and LLC members) to make broad investigatory requests.

FINRA / Broker-Dealer Updates

Changes in Expectations on Broker-Dealers' Responsibilities for Recommendations, Market Structure and Payment for Order Flow from the SEC under the Biden Administration

The SEC's agenda with respect to broker-dealers under the Biden administration and Chairman Gensler will highlight major issues and key differences from the previous administration in two important areas (1) broker-dealers' responsibilities in making recommendations and (2) market structure issues, including payment for order flow.

Broker-Dealer Recommendations

Regulation Best Interest ("Regulation BI"), Rule 151-1, currently requires a broker-dealer and its representatives to act in a retail customer's best interest when recommending a securities transaction or strategy, including an account recommendation, without placing either of their interests ahead of the customer. It has four components: (1) a disclosure obligation, (2) a duty of care, (3) a requirement for conflict management policies and procedures, and (4) a requirement for compliance policies and procedures. Both the broker-dealer and the salesperson must disclose, in writing, all material facts about their relationships with the customer, inlcuding the capacity in which they are acting, fees and costs of the transaction, the nature and extent of their services and their limitations, as well as conflicts associated with the recommendation. Each has to exercise reasonable diligence, care, and skill in making the recommendation—including understanding its risks, rewards, and costs in general and suitability to the customer in particular, without prioritizing their interests. The broker-dealer has to establish, maintain, and enforce written policies and procedures to identify, disclose, mitigate or eliminate different kinds of conflicts. Some conflicts, like sales contests and quotas, must be eliminated. And it has to have policies and procedures to achieve compliance with the rule, including the disclosure and due diligence obligations.

The obligation under Regulation BI is not a fiduciary duty. Democrats in Congress prefer to do away with it and impose on broker-dealers the same fiduciary duty for recommendations that applies to investment advisers. Congresswoman Maxine Waters, Chair of the House Financial Services Committee, has recommended that the rule be rescinded. However, it would be a significant legislative change, unlikely in the narrowly divided House and Senate with feelings just as strong on the other side of the aisle. The SEC can, of course, change the rule on its own to enhance the standard. So far, it has not signaled any intention other than to monitor and enforce strict compliance—not surprising given the effort expended and the politics involved. One thing to keep in mind, however, is that the SEC could, without any further action, simply apply existing legal interpretations that impose Advisers Act standards on broker-dealers that implicitly charge for recommendations or other advice, potentially affecting a wide variety of payment schemes in this era of little to no commissions for execution-only service.

It remains to be seen how enforcement of Regulation BI, which ascribes liability to the broker-dealer and its representatives, will play out. The violations themselves are essentially suitability infractions that historically have been handled by FINRA and state regulators. There is probably limited interest or utility in the SEC prosecuting those cases. The SEC may pursue individual-based infractions in particularly egregious cases; for example, a recent case involving a broker in New Hampshire that made unsuitable recommendations and churned the account of the State's former Governor, resulting in losses of more than $24 million. More likely, the SEC will bring cases against firms for systemic failures in due diligence and conflict management. The question is whether the SEC will focus on large-scale product or strategy failures—like the auction-rate securities debacle in 2008—or will use the rule to try to get ahead of those failures by requiring enhanced due diligence and disclosure before such calamities. The SEC already has

ample remedies at its disposal when securities recommendations are improper. However, it can use the rule effectively to impose heightened due diligence and disclosure requirements on broker-dealers without having to resort to rulemaking. The fact that there is no private right of action under Regulation BI limits the potential for expanded liability for broker-dealer firms.

For firms, protection against negligence-based liability under Regulation BI depends primarily on compliance with the policies and procedures elements, which determines how they meet their disclosure and due care responsibilities.

Market Structure and Payment for Order Flow

Senator Sherrod Brown, Chair of the Senate Banking Committee, has endorsed the *Better Markets* report, "Road to Recovery, Protecting Main Street from Dangerous Deregulation," issued in September 2020. The report is highly critical of the current market structure that it says is needlessly complex, fragmented and opaque. No major market structure reforms were on the SEC's agenda coming into the Biden administration. However, recent scrutiny of "payment for order flow," seen as both a symptom of and contributor to these conditions, in last year's *Robinhood* settlement and the SEC staff's recent investigation of retail trading in *GameStop* and other meme stocks, portends further regulations on the payments and heightened review of order execution quality and improper inducements to trade.

Payment for order flow is any benefit received by a broker-dealer from a market center for routing orders to the venue. The payment is in addition to any commissions or fees the broker-dealer charges to customers for executing the trades. A broker-dealer owes its customers a duty of best execution, which requires that it undertake to execute customer orders on the most favorable terms reasonably available, taking into account the potential for price improvement over the national best bid or offer (NBBO). The SEC recognizes that payment for order flow creates the potential for conflicts of interest in market selection. The payments are permissible, *provided,* that they do not interfere with the broker-dealer's best execution responsibilities and the practice is disclosed to customers. Arrangements that interfere with best execution may violate the anti-fraud provisions of the federal securities laws, as was found in the settlement with Robinhood Financial, LLC in December 2020. Robinhood agreed to pay a civil penalty of $65 million for inadequate disclosure relating to payment for order flow arrangements and misrepresentations about the quality of its executions stemming from those arrangements. Failure to disclose material facts about the arrangements also may violate Regulation BI.

Under agency law, a "broker" is a fiduciary for the execution of a customer's order, and generally must disclose and obtain specific consent to any remuneration or benefit obtained from another source pertaining to the relation or else it holds the benefit in trust for the customer. Compliance with the SEC's payment for order flow regime has been found to preempt state law challenges to the payments.

Under Rule 607 of Regulation NMS, a broker-dealer must inform customers, in writing, on account opening and annually thereafter, about (i) its policies on receiving payment for order flow, (ii) its order routing practices, and (iii) the extent to which its orders can receive price improvement. Confirmations for agency trades must disclose whether the firm received payment for order flow and advise that the source and nature of compensation is available on request. In addition, Rule 606 of Regulation NMS requires a broker-dealer to post quarterly reports on the percentages of non-client-directed orders in national market system (NMS) securities routed to its top 10 venues (plus any receiving 5% or more of the volume) with descriptions of "the material aspects of the relationship with each venue," including payment for order flow. Under amendments that took effect in 2019, the reports also must disclose (i) the net aggregate amount of payments received, (ii) transaction fees paid and (iii) rebates received, per venue. Descriptions of relationships with venues must include specific terms of payment for order flow arrangements,

including minimum order amounts, volume-based payments, and threshold incentives and disincentives. Separately, the broker-dealer must give notice and disclose to a customer on request payment for order flow information for its orders over the past six months, including (i) average net execution fee or rebate, (ii) average fee or rebate for providing liquidity, and (iii) average fee or rebate for removing liquidity.

In the past, descriptions of payment for order flow arrangements under Rules 606 and 607 were general. Rule 606 amendments require much more detailed disclosure—approaching the precise terms of payment arrangements with venues—which also should be considered for purposes of Rule 607. Reporting integrity can be expected to be the subject of increased attention in SEC and FINRA exams and enforcement.

Foreign Corrupt Practices Act

Although 2021 has not been a banner year for Foreign Corrupt Practices Act (FCPA) investigations and enforcement, the Biden administration has signaled a focus on anti-corruption with the Presidential memorandum in June 2021 establishing anti-corruption as a core national security interest, and the appointment of David Last, the-then acting chief of the Department of Justice's (DOJ's) FCPA Unit, as the permanent head in August 2021.

A handful of recent FCPA enforcement actions addressed conduct of financial services entities and individuals. In the first case, the DOJ entered into a deferred-prosecution agreement with a global investment bank and financial services company in connection with allegedly corrupt payments to a foreign official to obtain business with an investment vehicle indirectly owned by a foreign government. The DOJ noted the high-level management committees of the company approved the use of third-party intermediaries for consulting services but failed to address deficiencies regarding due diligence, oversight and documentation surrounding such arrangements raised by the company's internal audit reports. The company also settled a related case with the SEC.

The DOJ also filed several actions relating to an alleged bribery scheme involving illicit payments made to allow a group of US-based investment fund companies to act as custodian and investment adviser for certain Ecuadorian police social security funds. In February 2021, the DOJ filed a criminal complaint against the senior executive of the investment fund companies, generally alleging bribes in connection with a swap transaction where the fund manager received more money than the social security funds at the latter's expense, as well as a failure of the investment funds to meet their payment obligations on their bond repurchase agreements. An indictment was filed in October 2021 against both individuals, and in July 2021 a plea agreement and factual proffer were submitted by an employee of the clearinghouse and custodian for the social security investments.

In October 2021, a wholly owned subsidiary of a global investment bank pled guilty to wire fraud conspiracy and the bank entered into a deferred-prosecution agreement in connection with charges of conspiracy to commit wire fraud. The subsidiary acted as a joint lead manager underwriting the issuance of several hundred million dollars in loan participation notes and as joint dealer manager in the exchange of those notes for a sovereign bond. The DOJ alleged the global investment bank conspired with others to defraud investors and potential investors through numerous material misrepresentations and omissions relating to, among other things: (i) the use of loan proceeds, (ii) kickback payments to the bankers and the risk of bribes to foreign officials; and (iii) the existence and maturity dates of debt owed by the sovereign. In addition, the bank proceeded with the financing transaction although it had identified significant corruption and bribery concerns. Additionally, the bank failed to disclose when it became

aware of factors that raised the risk of default of the loan as well as a valuation shortfall identified by independent valuation experts.

Lastly, the SEC's whistleblower program rules were amended at the end of 2020 to expand award applicability to non-prosecution agreements and deferred-prosecution agreements. While the SEC does not disclose the underlying case details or subject matters for the whistleblower awards, the tipsters in two separate awards in 2021 indicated that they received their awards as a result of the FCPA enforcement actions.

Cases like these continue to demonstrate the need for continued monitoring and a rigorous response plan for potential FCPA red flags.

Antitrust/HSR

We have seen a number of noteworthy developments with respect to Hart-Scott-Rodino ("HSR") reporting and merger review more generally under the new administration and under new agency leadership in 2021. With the surge in M&A activity reportedly "straining" the Federal Trade Commission's resources, several new tactics have come into play that impact not only merger review and clearance, but also the way mergers are negotiated. While the close attention that Congress and the governmental agencies have been paying to antitrust will likely result in landscape shifts in enforcement policy and priorities for years to come, some of what has already been implemented and is already underway is making an immediate impact. The general approach has been a doubling down on enforcement, stripping away of exemptions and interpretations that make review more streamlined, and lengthier and more intrusive investigations. Some highlights include:

- Elimination of HSR early termination grants — requiring observance of the full 30-day HSR waiting period in all filed transactions;
- Issuance of "Warning Letters" at the close of HSR waiting periods;
- Withdrawal of long standing informal interpretations relating to HSR reporting, and public admonitions to the premerger office for issuance of so called "loophole" interpretations;
- Curtailing of parties' ability to exclude the value of outstanding debt from transaction value for HSR reporting obligation assessments;
- Withdrawal of long-standing informal interpretations relating to exclusion of copyright acquisitions from HSR reporting requirements;
- Withdrawal of the Vertical Merger Guidelines just only recently issued in 2020;
- Merger investigations that delve into historically off-limits areas, such as employee compensation, and issuance of "Second Requests" that are more broad reaching and invasive; and
- Consent decree provisions that are more onerous and restrictive.

Under the HSR Act, transactions that meet certain annually adjusted thresholds (currently a $92 million transaction size) are subject to notification and waiting period requirements. The FTC announced the new thresholds for 2021 effective March 4 — which decreased from $94 million to $92 million. The HSR Act enables antitrust regulators to review transactions, investigate and address potential competitive concerns prior to completion, and carries monetary penalties for failure to comply — also adjusted for 2021, to $43,792 per day.

Most transactions that meet the reporting requirements do not raise substantive antitrust concerns and are never investigated (typically around 90%), and the agency has historically terminated the statutory 30-day waiting period for most of those transactions in less than 30 days. Beginning in February 2021, the FTC suspended the longstanding practice of granting parties "early termination" of the 30-day waiting period for transactions it does not intend to investigate.

More recently, the agency has begun issuing letters to parties in certain transactions the agency may intend to investigate even *after* expiration of the HSR waiting period. Jurisdiction to conduct antitrust review of mergers and acquisition is independent of the HSR reporting requirements. This means that the enforcement agencies can investigate any transaction before or after closing, whether subject to reporting or not, and whether the HSR waiting period has expired or not. There are historical examples of the agencies using that authority to review non-reportable transactions, and even to open investigations of reportable transactions after expiration of the HSR waiting period — though these have been rare. The new practice of issuing warning letters to parties that an investigation may remain ongoing even post-HSR clearance has several important implications around the certainty or finality of investigation practices, and around obligations under parties' merger agreements with respect to closing potentially over a pending or ongoing investigation.

While the letters being issued do not assert any new authority not already existing under law, they are not being issued in every transaction. This means that the transactions for which the letters are issued are selected as ones that may raise more significant antitrust issues, and ones that the agency is more likely to investigate post-HSR waiting period and even post-closing — effectively putting merger parties on notice that the acquisition may face meaningful risk of agency action post-closing.

This, in turn, raises questions as to whether conditions are sufficiently satisfied to require the parties to close. A skittish buyer trying to assert that they are not required to close over a potential pending investigation may face an uphill battle depending on how the conditions to closing were drafted in the merger agreement. Such conditions typically point to the expiration of applicable waiting periods and not the absence of potential ongoing investigations. The FTC's new practice is already ushering in a change in the way certain provisions are drafted, with careful buyers seeking provisions that no investigations are open or pending and that no such warnings or warning letters have been issued.

Recent examples under the new policy include the 3D Systems Corporation/Oqton, Inc. transaction, where the parties' agreement provided that if the FTC or DOJ issued a warning letter that an investigation was pending beyond the expiration of the HSR waiting period, the investigation would be treated as closed only 30 days after receipt of such letter — if an active investigation was not pending. In another recent transaction, the parties' agreement likewise provided for an extension of the closing date by 30 days if the buyer receives a warning letter before closing.

Section 8 of the Clayton Act prohibits certain overlaps in officers or directors between competing companies to guard against anti-competitive coordination and information exchanges that can arise from simultaneous board membership. Thus, as a general rule, a person cannot serve on the boards of two competing companies, which can arise when installing board members of potentially competing portfolio companies. Under the statute, no person, or representative of the same person or entity, is permitted to serve simultaneously as a director or officer of competing companies, but there are carve-outs and exceptions. The prohibitions of Section 8 are limited to cases in which each of the companies has, under the revised thresholds for 2021, capital, surplus and undivided profits of more than $37,382,000. Even where the threshold is met, however, the restrictions do not apply if the competitive sales of *either* company represent less than 2% of its total sales, or are less than $3,738,200; or if the competitive sales of *each* company represent less than 4% of its total sales.

With antitrust enforcement of the technology sector making news daily, and lawmakers, enforcers and regulators all finding new ways to attack an industry that arguably is responsible for one of the greatest eras of advancement in history, knowing where the pitfalls are is the order of the day. To protect against buying the next antitrust headline, new areas of inquiry are required — beyond assessment of the combination's market shares. In addition to debt ratios, cap tables and pending litigation, good diligence now includes a clear assessment of the parties' business, their offerings and the markets implicated. This is necessary to evaluate whether either or both are in areas currently subject to enhanced antitrust scrutiny. Such areas can include diverse businesses such as platforms, e-commerce, internet infrastructure, social media, search, online advertising, streaming content and fintech.

Also consider whether the transaction would combine businesses that are in a vertical or vendor/vendee relationship. These can include, for instance, combinations of content producers or suppliers with content distributors. Transactions in this space can hit two areas that are presently the focus of what may be an undue level of agency attention — technology and vertical transactions. Vertical transactions can and do take place in all industries whenever two levels of a supply chain combine, such as manufacturer/distributor or distributor/retailer. While there is a long history of antitrust enforcement of *exceptional* vertical mergers that would lead to market foreclosure of inputs or distribution/sales channels, the trend now is to examine vertical mergers more closely as a matter of course. Add to this the FTC's recent withdrawal in September 2021 of the Vertical Merger Guidelines, issued and updated only recently in 2020 and criticized by the new FTC majority as based on "unsound economic theories that are unsupported by the law or market realities."

Historically, the FTC Premerger Notification Office has taken the view that the retirement of debt is not included in the calculation of whether a stock transaction meets the reporting threshold and is thus subject to the reporting and waiting period requirements of HSR. That position was reversed in August 2021, reportedly on the basis that "as a result of developments in deal structures and financing, sometimes the retirement of debt is part of the consideration for a transaction in that it benefits the selling shareholder(s)." Accordingly, in "any instance where selling shareholder(s) benefit from the retirement" of debt, the debt is considered part of the transaction consideration for purposes of assessing the parties' HSR reporting obligations. This is having immediate impact as we see reporting of transactions that historically would have not been subject to HSR filing requirements.

A number of changes have also been announced and implemented with respect to the FTC's merger investigation, or Second Request, process, including examination of how a proposed merger may impact labor markets, and "how the involvement of investment firms may affect market incentives to compete." Finally, in cases where merger parties settle with the agency on a challenge to the transaction rather than facing the agency in court, the consent decree process sets out the parties' obligations on a going forward basis. Historically, such consent decrees, among other things, required parties to notify the agency prior to certain future acquisitions implicating areas that are the subject of antitrust concern under the settlement. Beginning in October, 2021, however, the FTC consent decrees in such cases, beginning with its consent decree in the DaVita Inc. / Total Renal Care, Inc. transaction, now require prior approval before entering into such transactions: "IT IS FURTHERED ORDERED that Respondents shall not, directly or indirectly, through subsidiaries, partnerships, or otherwise, without the prior approval of the [FTC] . . . ." This is a significant policy change for the FTC and has the potential to chill not only settlements but also M&A transactions at the outset, where such provisions are commercially untenable.

Committee on Foreign Investment in the United States

The CFIUS landscape is very different from how things looked only a few years ago, and CFIUS continues to be an important issue and consideration for fund investors both inside the U.S. and abroad. With the enactment of FIRMA's updates to CFIUS in 2018, and the 2020 implementation of the new rules, 2021 is the first full year under the new regime. Some of the newer features of CFIUS now include:

- mandatory filings for certain transactions (limited to certain transactions implicating critical technology, critical infrastructure, and sensitive personal data);
- short, form declaration filings (now available for all transactions following a limited pilot program availability);
- CFIUS filing fees ($750 to $300,000 depending on transaction value);
- electronic filings;
- coverage of certain real estate investments and acquisitions involving proximity to sensitive government facilities and installations;
- expanded scope of critical infrastructure coverage;
- coverage with respect to sensitive personal data;
- expanded coverage of emerging and foundational technologies (*i.e.*, geospatial imagery software);
- expanded CFIUS identification and review of non-notified transactions;
- "White List" exempted investors for certain investors from UK, Canada and Australia; and
- country-specific application of certain rules related to critical technology.

For U.S.-based fund investors, CFIUS is often implicated by the presence of non-U.S. partners—co-investors, joint managers, or, to a lesser extent, in the LP base. The extent and scope of CFIUS coverage and jurisdiction turns on the type of rights granted to non-U.S. person or non-U.S. controlled entities, such as investment management discretion; GP removal rights; LPAC representation, board or observer rights; and certain information rights such as rights to Material Non-Public Technical Information. Non-U.S. fund investors and managers are more directly implicated in CFIUS coverage, though nationality matters to CFIUS and risk assessment is highly country specific.

CFIUS's appetite for clearing investments originating in certain parts of the world continues to wane. The ensuing chill in the investment climate has led to a sharp downward trend in filings specifically relating to investment originating in China (sometimes by way of the Cayman Islands) —down approximately 90% from just several years ago. Notably, many of the filings that relate to inbound investment from China focus on critical technology, one of the more sensitive areas of CFIUS review and a particular focus for the U.S. national security establishment. Though we're also seeing continued Chinese investment in U.S. critical infrastructure and in industries implicating sensitive personal. CFIUS does not evaluate issues relating to other foreign access to U.S. critical technologies, such as licensing, contracting or other arrangements that are not M&A related.

As the CFIUS and foreign investment review climate has not improved in the Biden administration from the prior administration, we expect to see continued lighter showing with respect to Chinese investment and continued chilly reception from the Committee. Consider the Biden administration's ongoing review of ByteDance's non-notified acquisition of Musical.ly (TikTok) initiated under the Trump administration. In

October 2021, CFIUS also opened an investigation into China-based Tencent's planned acquisition of Sumo Group, a UK-based producer of video games, as announced by the parties. CFIUS dos not publicly announce investigations or enforcement actions. CFIUS is likewise investigating China-based Wise Road Capital's proposed acquisition of Magnachip Semiconductor—by way of a Cayman affiliate. The parties did not initially file with CFIUS, and according to the company, on May 26, 2021, "the CFIUS Staff Chairperson, acting on the recommendation of CFIUS, requested that the parties file a notice concerning the Merger and thereby undergo formal CFIUS review of the Merger." The review and investigation is pending.

Though there is no public reporting with respect to specific transactions, filings or investigations, CFIUS identified for consideration an all-time high of 117 non-notified transactions the last reporting year, with 17 leading to formal filing and review. Such investigations can be costly and distracting for completed transactions, and at the margins can lead to undoing of completed deals. Thus, the better counselling under the current CFIUS climate is to file on a voluntary basis for transactions that are arguably likely to garner CFIUS's interest or attention. CFIUS also puts a high level of scrutiny on investors from Russia and certain Middle Eastern countries; however, largely as a function of primary investment flows, most of the filings still come from the lower-risk areas of Canada, UK, Japan, South Korea and Germany.

We continue to see sharp increases in short-form declaration filings, especially with respect to fund investors, as investors and practitioners become more comfortable with the newer process. The short-form declaration filings afford the added benefit of a shorter 30-day waiting and review period (versus 45 for the traditional joint voluntary notice long-form filing), though it is not always advisable for transactions likely to result in more in-depth investigations. This, plus an overall increase in the number of CFIUS filings more generally given the expanded scope of coverage areas, has led also to a smaller percentage of transactions that ultimately are subjected to remedies (or mitigation measures in CFIUS parlance) – hovering at around 10% of all filed transactions.

In the last available public reporting year, CFIUS implemented mitigation measures in approximately 20 transactions. Such mitigation measures typically include one or more of: restrictions on certain intellectual property, trade secret, or technical knowledge transfers; limiting access to information related to certain technology to only U.S. persons; assurances of continuity of supply to the U.S. Government; exclusion of certain sensitive assets from the transaction; prior notification and approval of future increases in ownership or additional rights; or ultimately, divestiture of all or part of the U.S. business. CFIUS's expanded mission, and staffing, also means that today we see at least some level of investigation on almost half of all submissions, which remain largely voluntary, with less than 20% of all filings falling into the mandatory filing requirement category.

The primary sectors subject to review continue to include utilities (such as power generation and infrastructure), computer system design (critical technology), software (especially encryption related software), financial services, transportation, aerospace, and industry (such as chemical manufacturing). Real estate investments remain a small minority of reported and reviewed transactions.

Anti-Money Laundering and Sanctions Enforcement Updates

Important Guidance from the Office of Foreign Assets Control

In October 2021, Treasury's Office of Foreign Assets Control (OFAC) released its 2021 Sanctions Review, which focused on: (1) the framework guiding the imposition of economic and financial sanctions and (2) potential operational, structural, and procedural changes to improve Treasury's ability to use sanctions now and in the future.

OFAC's review included steps Treasury should take to "modernize the underlying operational architecture by which sanctions are deployed" to effectively confront new and rising threats. Of particular importance to these modernization efforts is Treasury's development of capabilities in the digital assets space, which if left unchecked could harm the efficacy of OFAC sanctions.

The use of sanctions in the digital assets space is especially important given the growing threat that ransomware poses to the public and economy. In recent years, OFAC sanctions have increasingly targeted individuals and entities that have used virtual currency in connection with malign activity. For example, in September 2021, OFAC designated a Russian-based virtual currency exchange (SUEX) for facilitating financial transactions for ransomware actors.

In October 2021, OFAC released detailed guidance to help companies in the digital currency industry protect themselves from sanctions violations and the intentional misuse of digital currencies and platforms by actors attempting to evade sanctions and undermine U.S. foreign policy and national security interests. This guidance follows OFAC's issuance of an updated ransomware advisory on sanctions risks for making or facilitating ransomware payments, which discourages all private companies and citizens from paying ransom or extortion demands.

In both its guidance and ransomware advisory, OFAC notes that it can impose penalties for sanctions violations based on a "strict liability legal standard" meaning that a U.S. person can violate U.S. sanctions without having knowledge or reason to know it was engaging in a transaction that was prohibited under sanctions laws and regulations administered by OFAC. However, OFAC takes into consideration the "totality of facts and circumstances surrounding an apparent violation to determine the appropriate enforcement response." Important mitigating factors include (i) the strengthening of defensive and resilience measures to prevent and protect against ransomware attacks, (ii) the reporting of ransomware attacks to appropriate U.S. government agencies, and (iii) a company's implementation of a risk-based OFAC compliance program, which is outlined in A Framework for OFAC Compliance Commitments, published by Treasury in May 2019.

In its Framework, OFAC suggested for the first time that companies have an affirmative obligation to maintain an effective sanctions compliance program, which signaled that firms must now comply with OFAC's expectations by taking affirmative steps to understand and effectively address their sanctions risks.[1] Advisers to private funds should note this development, as all U.S. persons are required to comply with OFAC sanctions.

While failing to implement a sanctions compliance program is not itself a violation of OFAC's regulations, maintaining a sanctions compliance program has always been a mitigating factor in the assessment of

[1] For an in-depth discussion of OFAC's new compliance guidelines, see *Navigating the Complex Relationship Between Voluntary Self-Disclosure and Enforcement* by Seetha Ramachandran and Lucas Kowalczyk, in the International Comparative Legal Guide to Sanctions (2019).

monetary penalties in OFAC enforcement actions. A compliance program that falls short of the basic requirements outlined in OFAC's Framework may be viewed as a separate aggravating factor leading to increased monetary penalties in the event of a violation.

It is clear from the Framework that OFAC expects to see firms maintain more than just a check-the-box program. The guidance acknowledges that a firm's risk-based compliance program will depend on several factors, including the size and sophistication of firm, the products and services it offers, the nature of its customers and counterparties, and the geographic locations in which the firm operates. At the same time, OFAC identifies five essential components that every compliance program should incorporate: (1) support from senior management; (2) periodic risk assessments; (3) internal controls, including policies and procedures designed to identify, interdict, escalate, report, and maintain records related to activity that is prohibited by OFAC administered sanctions programs; (4) periodic testing and auditing; and (5) periodic training for all appropriate employees. In evaluating these criteria, OFAC appears focused on practical indicia that firms are committed to sanctions compliance, including how resources are allocated and the quality and experience of relevant personnel. Recent enforcement actions in the months following the guidance underscore OFAC's new emphasis on the importance of compliance programs.

In light of OFAC's Framework and recent guidance, advisers to private funds should take a hard look at their current sanctions compliance programs and consider implementing or enhancing existing procedures to attempt to ensure they do not engage in unauthorized transactions or with sanctioned persons or jurisdictions. In issuing penalties in 2020 and 2021, OFAC continued to recognize the presence of an OFAC compliance program in its settlements.

Focusing on sanctions compliance programs is particularly important as private funds continue to raise money offshore and pursue yield through foreign investments, and as the U.S. sanctions regime becomes more complex. In 2019, we saw changes to the sanctions against Russia, Venezuela, and Iran, which have had a significant impact on private funds. Also in 2019, the DOJ revised its policy for business organizations regarding voluntary disclosures of sanctions violations, signaling a continued push towards self-disclosure. In 2020 and 2021, the United States continued to promulgate new sanctions against Russia, Venezuela, and Iran, among others. OFAC is also increasingly taking the view that investment firms can be held directly responsible for the OFAC violations of foreign portfolio companies they may own and/or control.

SEC Examinations for Funds with an Affiliated Broker-Dealer or Investment Company

AML issues should also be top of mind for advisers to private funds that have an affiliated broker-dealer or investment company. In March 2021, the Division of Examinations announced its 2021 examination priorities. Just as it did in 2020, the Division stated it intends to "continue to prioritize examinations of broker-dealers and registered investment companies for compliance with their AML obligations." In particular, the Division intends to focus on whether firms are filing suspicious activity reports with Treasury's Financial Crimes Enforcement Network (FinCEN), as appropriate, and whether they have established appropriate customer identification programs and are conducting due diligence on customers. During examinations, the Division also intends to focus on whether firms are complying with beneficial ownership requirements, and conducting independent tests of their AML program on a timely basis. According to the Division, "[t]he goal of these examinations is to evaluate whether broker-dealers and registered investment companies have adequate policies and procedures in place that are reasonably designed to identify suspicious activity and illegal money-laundering activities." The SEC's continued focus on AML affects even those private funds that are not subject to a mandatory AML program rule, due to enhanced scrutiny facing fund affiliates, counterparties, and institutions that custody funds.

Potential areas for examination could include compliance with new beneficial ownership requirements, books and records requirements, and suspicious activity reporting. For example, in *SEC v. Alpine Securities Corp.*, the Southern District of New York suggested that the SEC's books-and-records authority under Exchange Act rule 17a-8, allows the SEC to bring enforcement actions based on the reporting of potentially suspicious transactions under the Bank Secrecy Act, expanding the SEC's jurisdiction over AML cases.

Over the last several years, the total amount of AML penalties imposed globally has been steadily rising, to more than $10.4 billion in 2020. Financial institutions in the United States took the brunt of the penalties in 2020, at $7.5 billion, led by a large investment bank, which was hit with nearly $7 billion in global fines in connection with three bond offerings the firm had structured and arranged for Malaysia's state development fund 1MDB. There has also been an increased focus on individual penalties of late – in 2020 over 200 individuals were fined nearly $90 million for related breaches.

The Financial Crimes Enforcement Network Updates Regulations Concerning the Bank Secrecy Act

2021 has been a transformative year for AML laws and regulations. On January 1, 2021, the United States Congress overrode then-President Donald Trump's veto of the National Defense Authorization Act for Fiscal Year 2021. The NDAA included, among other things, the Anti-Money Laundering Act of 2020 (the AMLA), which makes sweeping reforms to the Bank Secrecy Act. Part of the AMLA is the Corporate Transparency Act (the CTA) which, requires reporting companies to file a report with FinCEN that identifies the companies' beneficial owners and applicants. The purpose of the CTA is to "better enable critical national security, intelligence, and law enforcement efforts to counter money laundering, the financing of terrorism, and other illicit activity." The Secretary of Treasury must by regulation prescribe procedures governing reports and FinCEN identifiers by January 1, 2022.

Among other things, the CTA will require newly covered legal entities to report their beneficial owners at the time of their creation to a non-public database accessible by law enforcement, regulators, and U.S. financial institutions seeking to comply with their own AML compliance obligations. The change is designed in part to discourage the use of shell companies by money launderers or illicit actors. FinCEN issued an Advance Notice of Proposed Rulemaking in April of 2021 on the implementation of the new statutory requirements, and the final rule will be forthcoming, likely sometime in 2022.

In accordance with new requirements in the AMLA, on June 30, 2021, FinCEN published a new list of enforcement priorities to assist covered institutions to meet their obligations to combat money laundering and counter-terrorism financing. In order, the new priorities are: (1) corruption; (2) cybercrime, including relevant cybersecurity and virtual currency considerations; (3) foreign and domestic terrorist financing; (4) fraud; (5) transnational criminal organization activity; (6) drug trafficking organization activity; (7) human trafficking and human smuggling; and (8) proliferation financing.

The AMLA also enhanced DOJ and Treasury subpoena authority for non-U.S. bank records, so long as those banks hold correspondent accounts with U.S. financial institutions. Both DOJ and Treasury will now be able to demand information about any account from the foreign bank, including records maintained outside the United States.

Crypto-currencies will continue to be of interest to FinCEN in 2022, as the AMLA broadened various definitions throughout the BSA to include virtual currency, codifying previously issued guidance by the regulatory agency. And finally, the AMLA substantially increased penalties for BSA violations.

On the rulemaking front, on March 11, 2021, FinCEN issued an advisory to inform financial institutions of updates to the Financial Action Task Force's ("FATF") list of jurisdictions with strategic deficiencies in their regimes regarding anti-money laundering, combating the financing of terrorism and counter-proliferation financing. Financial institutions should review FATF statements regarding their obligations and risk-based policies, procedures, and practices while dealing with relevant jurisdictions.

On September 23, 2021, FinCEN issued an Advance Notice of Proposed Rulemaking to solicit public comment on a range of questions related to the implementation of the new amendments to the BSA regarding the trade in antiquities. Section 6110 of the AML Act amended the BSA by including as a type of financial institution a person engaged in the trade of antiquities, including an adviser, consultant, or any other person who engages as a business in the solicitation or the sale of antiquities. The trade in antiquities may be exploited by money launderers and terrorist financiers to evade detection by law enforcement and to launder their illicit funds through the U.S. financial system. Terrorist organizations, transnational criminal networks, and other malign actors may also seek to exploit antiquities to transfer value to acquire new sources of funds, evade detection, and launder proceeds from their illicit activities. Some terrorist groups have generated revenue from permitting or facilitating the illegal extraction or trafficking of antiquities in territories where they operate. Comments closed on the Proposed Rulemaking in October and a final rule should be forthcoming.

On October 15 and November 8, 2021, FinCEN published financial trend analysis focusing on ransomware patterns and trend information identified in Bank Secrecy data between January 2021 and June 2021. The analysis demonstrated that ransomware is an increasing threat to the U.S. financial sector, businesses, and the public. The total number of SARs from January 1, 2021 to June 30, 2021 was 30% higher than the total for the entire 2020 calendar year. The total value of suspicious activity reported in ransomware-related SARs during the first six months of 2021 was $590 million, exceeding the value reported for all of 2020 ($416 million). Accordingly, FinCEN recommended that financial institutions: (1) incorporate Initial Operating Capabilities ("IOCs") from threat data sources into intrusion detection systems and security alert systems to block or report suspected malicious activity; (2) contact law enforcement immediately regarding any ransomware activity, and contact the Office of Foreign Assets Control if there is any reason to suspect the cyber actor demanding ransomware payment may be sanctioned or have a sanctions nexus; (3) report suspicious activity to FinCEN; and (4) review FinCEN's October 1, 2020 advisory on financial red flag indicators of ransomware mentioned above.

Cayman Islands Anti-Money Laundering Developments

Advisers to Cayman Islands-based funds should confirm that they are in compliance with Cayman Islands AML regulations that went into effect in 2018. The 2018 regulations altered the regulatory environment for Cayman Islands-based funds, including those that are unregistered. One of the major changes in the Cayman Islands AML regulations is a new requirement that Cayman Islands funds designate natural persons employed at a managerial level to serve as AML officers. Specifically, Cayman Islands funds are now required to designate an AML Compliance Officer, a Money Laundering Reporting Officer, and a Deputy Money Laundering Reporting Officer. The new Cayman Islands AML regulations also significantly expand the kinds of AML procedures that funds are expected to maintain.

U.S. Tax

"Build Back Better" Budget Reconciliation Bill

On September 13, 2021, the House Ways and Means Committee introduced a reconciliation bill (the "House Bill") that would generally increase tax rates for individuals and corporations, substantially revise the U.S. international tax regime, and otherwise reduce certain tax benefits for individuals earning over $400,000. On October 28, 2021, the House Rules Committee published a revised version of the bill containing significant amendments to its earlier iteration. The House of Representatives passed the Build Back Better Act (H.R. 5376 or the "Act"), a $1.75 trillion legislation, on November 19, 2021. The bill now faces debate in the Senate chamber, where it will likely be altered.

Certain provisions that received widespread attention earlier in the year, such as the proposals to change the treatment of carried interest and raise the top marginal individual and corporate income tax rates, were not included in the version of the bill passed in the House. Additionally, the Act excludes the following other provisions that were in earlier versions of the Act or proposed by lawmakers:

- Increase of the capital gains rate from 20% to 25%
- Repeal of the "pass through deduction" under Section 199A for taxpayers making more than $400,000
- Allowance for an S corporation that made an S corporation election on or before May 13, 1996 to reorganize as a partnership in the two-year period beginning on December 31, 2021 without recognizing gain
- Limitations on like-kind exchanges
- Taxation of unrealized gains at death or repeal of the step-up in basis of assets
- Restrictions on estate tax valuation discounts

Summary of Significant Changes in the Most Recent Version of the Act

A brief summary appears below with detailed discussion to follow:

Corporate taxation

- The imposition of a 15% alternative minimum tax on C corporations with an average annual adjusted financial statement income over $1 billion over a certain period.
- The imposition of a 1% excise tax on corporate stock repurchases.
- The interest expense deduction of a domestic corporation that is part of an "international financial reporting group" and whose average annual net interest expense exceeds $12 million over a three-year period would be disallowed to the extent its net interest expense for financial reporting purposes exceeds 110% of its proportionate share (determined based on its share of the group's EBITDA) of the net interest expense for financial reporting purposes of the group. The disallowed interest deduction could be carried forward for five years.
- Losses recognized by a corporate shareholder in liquidation of its majority owned corporate subsidiary would be deferred until substantially all of property received in the liquidation is disposed of by the shareholder.
- Corporations spinning off subsidiaries would be limited in their ability to use debt of the subsidiary to receive tax-free cash.
- Modification of the real estate investment trust ("REIT") constructive ownership rules by providing that stocks, assets, and net profits constructively owned by a partnership, estate, trust, or corporation by reason of Section 318(a)(3) "downward" attribution are not considered as owned by the entity for purposes of again applying Section 318(a)(3).

Individual taxation

- A 5% or 8% surcharge on individuals, estates, and trusts with a modified adjusted gross income above certain thresholds.
- The exemption of gains on the disposition of qualified small business stock would be reduced from 100% to 50% for taxpayers earning more than $400,000/year, and trusts and estates.
- The 3.8% net investment income tax ("NIIT") would be expanded to apply to the active trade or business income of taxpayers earning more than $400,000. Under current law, the NIIT applies only to certain portfolio and passive income.
- The limitation on deducting "excess business losses" in excess of $250,000 ($500,000 in the case of a joint return) would be made permanent. This provision currently is scheduled to expire at the end of 2026.
- Losses recognized with respect to worthless partnership interests would be limited.
- The wash sale rules would be expanded to cover cryptocurrency, digital assets, and dispositions by parties related to the taxpayer.

International taxation

- The Act would substantially revise the various international tax rules enacted as part of the Tax Cuts and Jobs Act ("TCJA"), including "GILTI," "FDII" and "BEAT" regimes.
- Changes to the Section 250 deduction for "foreign-derived intangible income" ("FDII").
- Expansion of the "base erosion and anti-abuse tax" ("BEAT").
- Changes to the Subpart F regime.
- Foreign tax credit limitation rules would be substantially revised to be applied on a country-by-country basis.
- Section 871(m), which imposes U.S. withholding tax on U.S.-dividend equivalent payments on swaps and forwards, would be expanded to require withholding on the U.S. "specified partnership interest income equivalent payments" that are made with respect to, or by reference to, interests in publicly traded partnerships.
- Modification of the portfolio interest exemption.

Discussion

Corporate Tax Changes

Minimum tax for certain corporate taxpayers

Effective December 31, 2022, a 15% alternative minimum tax ("AMT") would apply to corporations (except S corporations, RICs, and REITs) with more than $1 billion in annual adjusted financial statement income (averaged over three years).

Excise tax on stock repurchases

There would be a 1% excise tax on the fair market value of stock buybacks by publicly traded corporations. There would be certain exceptions to this excise tax, including repurchases taxed as dividends to the shareholder.

Limitation on business interest expense deductions

The Act would introduce an additional interest deduction limitation for a U.S. corporate member of an international group that has disproportionate interest expense as compared to the other members of the group. New Section 163(n) would generally limit the interest deduction of a U.S. corporation that is part of an "international financial reporting group" and has net interest expense that exceeds $12 million (over a

three-year period) if the ratio of its net interest expense to its EBITDA exceeds 110% of the similar ratio for the group.

Proposed Section 163(n) is similar to a proposal that was included in the Senate and House bill for TCJA that was ultimately dropped in the conference agreement between the Senate and the House. This limitation appears to target base erosion interest payments that may not be captured under the BEAT regime (which is further discussed in detail below).

The Act would also revise Section 163(j) to treat partnerships as aggregates for purposes of applying the business interest expense limitation. As a result, the Section 163(j) limitation would be applied at the partner level instead of at the entity level.

Limitation on loss recognition in corporate liquidations

The Act would defer the loss that is recognized by a corporate member of a controlled group when a subsidiary merges into it in a taxable transaction under Section 331 until substantially all of the property received in the liquidation is disposed of to a third-party. This proposal effectively eliminates taxpayers' ability to enter into *Granite Trust* transactions to recognize capital losses by liquidating an insolvent subsidiary.[2]

Limitation on using controlled corporation's debt in a spin-off transaction

The Act would limit the ability of a U.S. "distributing corporation" to effectively receive cash tax-free from a spun-off "controlled corporation" subsidiary. Under current law, a controlled corporation can issue debt securities to its parent distributing corporation that the distributing corporation can then use to redeem its own outstanding debt on a tax-free basis in connection with the spin-off of the controlled corporation. The Act would require the parent distributing corporation to recognize gain in this transaction to the extent that the amount of controlled corporation debt it transfers to its creditors exceeds (x) the aggregate basis of any assets it transfers to its controlled corporation in connection with the spin-off, less (y) the total amount of liabilities the controlled corporation assumes from it, and (z) any payments that the controlled corporation makes to it. This effectively treats the debt securities issued by a controlled corporation the same as any other property distributed by the controlled corporation (which is commonly known as "boot").

REIT ownership rules

Rents from real property are considered "good income" for a REIT. Rents are not treated as rents from real property if the REIT owns stock possessing 10% of the vote or value of a corporate tenant or an interest of 10% or more in the assets or net profits of a partnership tenant, as applicable. For purposes of determining the ownership of stock, assets, or net profits, the constructive ownership rules of Section 318(a) apply except that "upward" attribution (attribution from a corporation) and "downward" attribution (attribution to a corporation) apply if 10% (rather than 50%) of the vote or value of the corporation is owned, directly or indirectly, by or for any person. These attribution rules may inadvertently cause a tenant of a REIT to be related to the REIT, causing the tenant's rent to fail to be "rents from real property" and potentially causing the REIT to fail the REIT income test.

The Act would modify the REIT constructive ownership rules by providing that stock, assets, and net profits constructively owned by a partnership, estate, trust, or corporation by reason of Section 318(a)(3) "downward" attribution are not considered as owned by the entity for purposes of again applying Section 318(a)(3).

[2] In a Granite Trust transaction, a corporate parent that owns a depreciated subsidiary reduces its ownership in the subsidiary to below 80% before liquidating the subsidiary so that the liquidation is taxable and any built-in loss of the parent in the subsidiary's stock would be recognized.

Individual Tax Changes

Surtax on high income taxpayers

The bill proposes a 5% tax on modified adjusted income ("MAGI") greater than $10 million, with another 3% tax to apply to MAGI above $25 million.

Limitation on qualified small business stock benefits

The Act would limit the exemption of eligible gain from the disposition of qualified small business stock ("QSBS") to 50% for taxpayers with adjusted gross income of $400,000 or more, as well as trusts and estates.

Very generally, non-corporate taxpayers are entitled to tax-free treatment with respect to the greater of (i) $10 million of gain and (ii) gain equal to 10 times the taxpayer's aggregate adjusted tax bases of QSBS from the disposition of QSBS that has been held for more than 5 years.

Expansion of the 3.8% NIIT

The Act would expand the NIIT to apply to net income derived in an active trade or business of the taxpayer, rather than, under current law, only to certain portfolio income and passive income of the taxpayer.

As a result, the 3.8% NIIT would be imposed on limited partners who traditionally have not been subject to self-employment tax on their distributive share of income, and S corporation shareholders who have not been subject to self-employment tax on more than a reasonable salary. This proposed change is generally consistent with the Biden administration's proposal to impose 3.8% Medicare tax (although the additional NIIT proposed in the Act would not be used to fund Medicare).

The Act also would limit the NIIT tax so that it applies only to taxpayers with taxable income greater than $400,000 (and $500,000 in the case of married individuals filing a joint return), rather than $250,000 under current law.

The changes would apply in taxable years beginning after 2021.

Excess business losses

Under current law, for taxable years that begin before January 1, 2027, non-corporate taxpayers may not deduct an excess business loss (generally, net business deductions over business income) if the loss is in excess of a certain threshold amount, (beginning at $250,000 in 2018 (or $500,000 in the case of a joint return), and indexed for inflation each year). The excess loss becomes a net operating loss in subsequent years and is available to offset 80% of taxable income each year. The Act would make this limitation permanent and would treat any loss carried forward to the next taxable year as a deduction attributable to a trade or business, which would be subject to the excess business loss limitation. As a result, any excess business losses would no longer become net operating losses.

Worthless partnership interests

Under current law, if a partner's interest in a partnership becomes worthless, in the taxable year of worthlessness, the partner may take either an ordinary loss if the partner has no share of any liabilities of the partnership immediately prior to the claim of worthlessness or a capital loss if the partner has a share of any partnership liability immediately prior to the claim of worthlessness (because relief of partnership liabilities is treated as consideration received in a sale). Under current law, if a security (not including an obligation issued by a partnership) that is held as a capital asset becomes worthless, the loss is treated as occurring on the last day of the taxable year in which the security became worthless.

Under the Act, if a partnership interest becomes worthless, the resulting loss would be treated as a capital loss (and not an ordinary loss). Also, in the case of a partnership interest or a security that becomes worthless, the loss would be recognized at the time of the identifiable event establishing worthlessness (and not at the end of the taxable year). The proposal would also expand securities subject to the worthless securities rule to include obligations (bond, debenture, note, or certificate, or other evidence of indebtedness, with interest coupons or in registered form) issued by partnerships.

Expansion of wash sale and constructive sale rules

The Act would expand the application of the wash sale rules and constructive sale rules to cryptocurrencies and other digital assets.

The Act would also expand the wash sale rules to include transactions made by related parties. The wash sale rules disallow a loss from a sale or disposition of stock or securities if the taxpayer acquires or enters into a contract to acquire substantially similar stock or securities thirty days before or after the sale giving rise to the claimed loss. The basis of the acquired assets in the wash sale is increased to include the disallowed loss. Under the Act, a wash sale would also occur when a "related party" to the taxpayer (other than a spouse) acquires the substantially similar stock or securities within the thirty-day period. More significantly, the disallowed loss in a wash sale triggered by a related party (other than a spouse) would be permanently disallowed under the Act. It would be very difficult for taxpayers to comply with this change, and very difficult for the IRS to enforce it. For example, under the provision, if a parent were to sell stock at a loss and, within 30 days, her child were to purchase the same stock, the parent's loss would be denied, even if neither parent nor child knew about each other's trades.

Finally, the Act would provide that an appreciated short sale, short swap, short forward, or futures contract is constructively sold under Section 1259 when the taxpayer enters into a contract to acquire the reference property (and not when the taxpayer actually acquires the reference property, as current law provides).

International Tax Changes

GILTI

The "global intangible low-taxed income" ("GILTI") regime generally imposes a 10.5% minimum tax on 10-percent U.S. corporate shareholders of "" controlled foreign corporations" ("CFCs") based on the CFC's "active" income in excess of a threshold equal to 10% of the CFC's tax basis in certain depreciable tangible property (such basis, "qualified business asset investment," or "QBAI"). GILTI is not determined on a country-by-country basis, and, therefore, under current law a U.S. multinational corporation may be able to avoid the GILTI tax with respect to its subsidiaries operating in low-tax rate countries by "blending" income earned in the low tax-rate countries with income from high-tax rate countries. Taxpayers are allowed 80% of the deemed paid foreign tax credit with respect to GILTI.

The Act would impose GILTI on a country-by-country basis to prevent blending of income from a low tax-rate country with income from a high-tax rate country. This general approach is largely consistent with the proposals made by the Biden administration and the Senate Finance Committee.[3]

The Act would determine net CFC tested income and losses and QBAI on a country-by-country basis. The Act would achieve this by using a "CFC taxable unit" – net CFC tested income and loss would be determined separately for each country in which a CFC taxable unit is a tax resident. The Act would

[3] The Senate Finance Committee's proposal provided for a mandatory exclusion of high-taxed income. This approach is different from the Act, but the general approach of disallowing "blending" of income between high-tax jurisdictions and low-tax jurisdictions is the same.

allow a taxpayer to carryover country-specific net CFC tested losses to a succeeding tax year to offset net CFC tested income of the same country.

Under the Act, taxpayers would no longer be able to offset net CFC tested income from one jurisdiction with net CFC tested losses from another jurisdiction.

The Act would also (i) reduce the exclusion amount from 10% to 5% of QBAI, (ii) increase the effective tax rate on GILTI for corporate taxpayers from 10.5% to 16.5625%[4] and (iii) helpfully (and retroactively to 2018) reduce the "haircut" for deemed paid foreign tax credit for GILTI from 20% to 5% (i.e., 95% of the GILTI amount would be creditable as deemed paid credit).

FDII

The "foreign-derived intangible income" ("FDII") regime encourages U.S. multinational groups to keep intellectual property in the U.S. by providing a lower 13.125% effective tax rate for certain foreign sales and provision of certain services to unrelated foreign parties in excess of 10% of the taxpayer's QBAI. The lower effective tax rate is achieved by a 37.5% deduction allowed for FDII under Section 250.

The Act would reduce the Section 250 deduction for FDII from 37.5% to 24.8%, which would have the effect of increasing the effective rate for FDII from 13.125% to 15.8%. The Act further provides that if a Section 250 deduction actually exceeds the taxable income of the taxpayer, the deduction would increase the net operating loss amount for the taxable year and could be used in subsequent years to offset up to 80% of taxable income.

BEAT/SHIELD

The "base erosion and anti-abuse tax" ("BEAT") generally provides for an add-on minimum tax, currently at 10%, on certain deductible payments that are made by very large U.S. corporations (generally, with at least $500M of average annual gross receipts) whose "base erosion percentage" (generally, the ratio of deductions for certain payments made to related foreign parties over all allowable deductions) is 3% or higher (or 2% for groups that include banks and securities dealers).

The Act would expand the BEAT regime. The proposal would increase the BEAT tax rate gradually from 10% up to 18% by the taxable year starting after December 31, 2024. The proposal would also substantially revise the formula for calculating "modified taxable income," which generally appears to increase the income amount that would be subject to the BEAT regime. Finally, the Act would eliminate the 3%/2% de minimis exception.

Notably, the Act does not include the Biden administration's "Stopping Harmful Inversions and Ending Low-Tax Developments" ("SHIELD"). The Biden Administration had proposed to repeal the BEAT regime and replace it with the SHIELD regime, but the details on the SHIELD regime had not been provided by the Biden Administration.

Changes to the Subpart F regime

The Act would significantly change the Subpart F regime. The Act would helpfully reinstate Section 958(b)(4). Section 958(b)(4) had prevented "downward" attribution of ownership by a foreign person to a related U.S. person for purposes of applying the Subpart F regime. Section 958(b)(4) was repealed in the TCJA, which allowed stock owned by a foreign person to be attributed downward to a U.S. person for purposes of determining a foreign corporation's CFC status. The repeal was intended to prevent certain taxpayers from "de-controlling" their CFCs and avoid paying current tax on the earnings of those CFCs. However, it inadvertently caused a number of foreign corporations to be treated as CFCs for U.S. federal

[4] This would be achieved by reducing the deduction provided to corporate taxpayers under Section 250 from the current 50% level to 37.5%. The Act would not change the tax rate to be applied to a non-corporate taxpayer's GILTI amount.

income tax purposes and gave rise in certain circumstances to some adverse tax consequences (for a more in-depth discussion on issues that arose as a result of the repeal of Section 958(b)(4), please refer to our blog post on the subject).

To address the situation that had prompted the repeal of downward attribution, the Act would introduce a new section to apply GILTI and the Subpart F regime to a foreign corporation that would be a CFC if the downward attribution rule had applied, but only if the U.S. shareholder holds at least 50% of the vote or value of the foreign corporation's stock. The Act would also allow a U.S. shareholder of a foreign corporation to elect to treat it as a CFC, which may permit a taxpayer to exclude foreign-source dividends received from the foreign corporation under the Act's amended Section 245A (which is discussed below). The Act also (i) limits the scope of foreign base company sales and services income, which is includible as Subpart F income, to sales and services provided to U.S. residents and pass-through entities and branches in the United States, which effectively would subject foreign base company sales and services income for non-U.S. sales and services to the GILTI regime, and (ii) amends Section 951(a) so that a United States shareholder that receives a dividend from a CFC would be subject to tax on its pro rata share of the CFC's Subpart F income (generally negating any deduction under Section 245A with respect to the dividend), regardless of whether the shareholder holds shares in the CFC on the last day of the CFC's taxable year. Current law requires a United States shareholder to include Subpart F income only if it owned shares in the CFC on the last day of the CFC's taxable year.

Foreign tax credits

The Act would impose the foreign tax credit limitation on a country-by-country basis. Currently, foreign tax credits are calculated on an aggregate global basis and divided into baskets for active income, passive income, GILTI income, and foreign branch income. The revised rules would calculate foreign tax credit limitations based on a country-by-country "taxable unit," which is consistent with the "CFC taxable unit" used under the Act's GILTI rules discussed above. Together with the proposed amendments to the GILTI regime, this revision to the foreign tax credit limitation rules seeks to prohibit taxpayers from using foreign tax credits from taxes paid in a high-tax jurisdiction against taxable income from a low-tax jurisdiction.

The Act would make a number of other changes to the foreign tax credit rules, including limiting the carryforward period for excess foreign tax credit limitation to 5 years (compared to 10 years under current law) and repealing the carryback period (which, under current law, is 1 year).

Dividends from foreign corporations

The Act would amend Section 245A so that the foreign portion of dividends received only from a CFC (rather than any specified 10% owned foreign corporation) would qualify for the participation exemption (and not be subject to U.S. federal income tax) under Section 245A. Currently, Section 245A allows foreign-source dividends from any specified 10% owned foreign corporation (a broader concept than CFC) to be exempt from U.S. tax under Section 245A. Although the provision appears to narrow the scope of Section 245A, as noted above, the Act permits a taxpayer and a foreign corporation to make an election to treat the foreign corporation as a CFC, in which case the benefits of Section 245A would be available to all dividends paid by the electing foreign corporation (even if U.S. shareholders own less than 10%). This provision would be retroactively effective for taxable years of foreign corporations beginning after December 31, 2017.

Portfolio interest exemption

The portfolio interest exemption, which eliminates U.S. withholding on outbound interest payments under certain conditions, does not apply where the non-U.S. recipient is a "10% shareholder" of the obligor. Current law permits so called "high vote/low vote structures," under which the sponsor of a fund will typically invest 5% of the capital of a U.S. blocker in exchange for 91% of the vote, thereby ensuring that no foreign investor will own 10% of the voting power of the U.S. blocker and permitting those foreign investors who own more than 10% of the value of the U.S. blocker to avoid U.S. withholding tax on

interest received from the U.S. blocker. The Act would revise this exception so that any person who owns 10% or more of the total voting power or value of the stock of a corporate issuer would be ineligible for the portfolio interest exemption. Funds utilizing these high vote/low vote structures may wish to consider the impact of these changes and, if there is a significant modification of an existing loan for U.S. federal income tax purposes or if there could be further drawdowns on an existing loan, whether a restructuring may be warranted.

Subchapter K Proposals

Senator Ron Wyden had proposed a detailed proposal of significant changes to the partnership tax rules one week before the House Ways and Means Committee proposal (which became the Act) was released. Although it appears, at this time, unlikely that there will be any sort of comprehensive partnership tax reform, one or more of the proposals could find their way into the final tax bill or be reintroduced in a future bill. Some of the major proposals included in the current bill are:

- The "substantial economic effect" safe harbor for allocations would be repealed and all partnership allocations would be tested under the "partner's interest in the partnership" standard.
    - Under current law, a partnership's allocations will be respected if they satisfy the substantial economic effect safe harbor or otherwise are consistent with the partners' interests in the partnership. There is very little authority on the meaning of a partner's interest in the partnership and, therefore, the standard presents great uncertainty.
- The "remedial method" for Section 704(c) allocations would be mandated for built-in gain properties.
    - Under current law, if a partner contributes an appreciated asset to a partnership, the difference between the fair market value on the date of contribution and the contributing partner's basis is "Section 704(c) gain," which is intended to be taxed over time to the property contributor. The regulations permit alternative ways of allocating (and therefore taxing to the contributor) the Section 704(c) gain. Under the "traditional method," the Section 704(c) gain is not allocated until a sale or disposition of the underlying asset. Under the "remedial method," income and offsetting deductions are created each year, and the income is allocated to the contributing partner (and the deductions to the other partners).
    - While the remedial method best matches taxable income to economic income, it could give rise to "phantom income" to the contributing partner (i.e., taxable income without the cash to pay the tax) and is administratively complex.
- A partner that contributes a built-in gain property to a partnership would be required to recognize gain if the property is at any time subsequently distributed to another partner or the contributing partner is distributed other property. Under current law, gain is not required to be recognized if the property (or other property) is distributed more than seven years after it was contributed.
- A partnership would not terminate for tax purposes if any part of the business is carried on by a former partner of the partnership or any person related to any of the former partners.

  Partnership debt would be required to be allocated in accordance with partners' respective share in partnership profits (as opposed to the current allocation rules based on economic risk of loss of the partners). Under current law, partners have a good deal of flexibility on how to allocate partnership debt among the partners. The proposal would constrain that flexibility.

Introduction of the Ending of the Carried Interest Loophole Act

As mentioned above, the Act does not include any proposed changes to the treatment of carried interest, despite recent efforts by some lawmakers to change the way carried interest is taxed. Notably, on August 5, 2021, Senators Ron Wyden and Sheldon Whitehouse introduced the bill know as Ending the Carried Interest Loophole Act, which would require that investment fund managers, partners, and others who hold carried interests in connection with their services to investment partnerships include as ordinary income a certain amount of deemed compensation each year.

The proposed legislation would go further than changes enacted under the TCJA, which extended the holding period required for long-term capital gain treatment to three years for certain interests (codified in Section 1061). The September release of the Act contained a provision to extend the current three-year holding period to five years for any interest holders with adjusted gross incomes in excess of $400,000. However, the provision was eliminated in the October 2021 version of the bill.

Wyden's bill applies only to applicable partnership interests as defined in Section 1061 and relies on a set-up involving a hypothetical interest-free loan. Under the bill, the carried interest holder is treated as if it had received compensation in the amount of foregone interest – this "deemed compensation" being characterized and taxed as ordinary income on an annual basis.

The bill would repeal Section 1061. Additionally, under the bill, a partner receiving a partnership interest in connection with the performance of services would be treated as making a Section 83(b) election unless the partner timely opts out of the election.

IRS Issues Final Regulations on the Taxation of Carried Interest Under Section 1061

On January 7, 2021, the IRS and the Treasury issued final regulations providing guidance on Section 1061 of the Code (the "Final 1061 Regulations"). The Final 1061 Regulations modify the proposed regulations (the "Proposed 1061 Regulations") that were released in July of 2020 (for a discussion of the Proposed 1061 Regulations, please see our August 6, 2020 client alert published here). The following highlights certain changes made to the Proposed 1061 Regulations and certain important provisions of the Proposed 1061 Regulations that remain unchanged in the final regulations:

In general, Section 1061 requires a three-year holding period for an investment fund manager's share of capital gains earned through a fund to be eligible for the lower tax rates applicable to long-term capital gain. This is a departure from the one-year holding period that is typically required for long-term capital gain treatment. The Proposed 1061 Regulations provided some guidance on the application of Section 1061; however, many of the provisions in the Proposed 1061 Regulations required clarification and further guidance.

The Final 1061 Regulations are generally helpful to taxpayers, except with respect to allocations of unrealized gain, as discussed below. However, some questions remain unresolved and fund managers should continue to exercise care in interpreting and applying the Final 1061 Regulations.

Changes introduced by the Final 1061 Regulations:

Expansion of the capital interest exception

Section 1061 applies to an applicable partnership interest (an "API") held by or transferred to a taxpayer in connection with the performance by that taxpayer (or a related person) of substantial services in an applicable trade or business. Section 1061 provides an exception for gain with respect to "capital interests" (generally understood to mean gain earned with respect to invested capital). The Proposed 1061 Regulations narrowly defined the scope of this exception, but the Final 1061 Regulations provide more flexibility.

Under the Proposed 1061 Regulations, the capital interest exception applied only to allocations in respect of a fund manager's capital if those allocations were made in the "same manner" as allocations made to other unrelated non-service partners with a "significant" aggregate capital account balance in a fund (defined as at least 5% or more of the aggregate capital account balances of the partnership). An allocation would be considered to be made in the "same manner" if the allocation were based on the relative capital account balances of the partners and the terms, priority, type, level of risk, rate of return, and rights to cash or property distributions during the partnership's operations and liquidation were the same.

The Final 1061 Regulations replace the "same manner" requirement with a "similar manner" requirement, where allocation and distribution rights with respect to fund managers' capital interests must now be "reasonably consistent" with such rights applicable to limited partners with a "significant" aggregate capital account balance in a fund (still defined as at least 5% or more of the aggregate capital account balances of the partnership). The similar manner test may be applied on an investment-by-investment basis or on the basis of allocations made to a particular class of interests.

Finally, the Final 1061 Regulations explicitly confirm that a fund manager's capital interest will not be ineligible for the capital interest exception solely because that fund manager is not charged management fees or carried interest, or because a fund manager has a right to receive tax distributions but unrelated non-service partners do not have such a right, so long as such distributions are treated as advances against future distributions.

Treatment of capital interests acquired with loan proceeds

The Final 1061 Regulations retain the general rule set forth under the Proposed 1061 Regulations that the capital interest exception does not apply to capital funded with the proceeds of a loan made or guaranteed, directly or indirectly, by the partnership, a partner or any person related to the foregoing. However, the Final 1061 Regulations helpfully contain an exception to this general rule that allows capital interests of an individual service provider acquired with loan proceeds made, directly or indirectly, by any partner or any related person (other than the partnership) to still qualify for the capital interest exception so long as the individual service provider is personally liable for the repayment of such loan or advance. The Final 1061 Regulations further provide that an individual service provider is considered personally liable for the repayment of a loan or advance made by a partner (or any related person, other than the partnership) if (i) the loan or advance is fully recourse to the individual service provider, (ii) the individual service provider has no right to reimbursement from any other person, and (iii) the loan or advance is not guaranteed by any other person.

Treatment of unrealized gain

Some commentators had questioned whether, under the Proposed 1061 Regulations, unrealized gains that were allocated to a fund manager's capital account as a result of a "book-up" or other revaluation event could be treated as capital of the fund manager for purposes of the capital interest exception (in other words whether a fund manager could get "credit" for economic, untaxed gains in its capital account for purposes of the capital interest exception).

The Final 1061 Regulations clarify that gains must be realized before a fund manager receives credit for purposes of the capital interest exception, and, therefore, a fund manager cannot get "credit" for unrealized gains. The Final 1061 Regulations provide that any such realized gains will be treated as reinvested for these purposes whether such realized gains are distributed and recontributed to the fund by the fund manager or retained by the fund manager in the fund.

Transfers of APIs to related persons

Section 1061(d) generally provides that, if a taxpayer transfers, directly or indirectly, any API that has been held for three years or less, to a person related to the taxpayer (defined to include a taxpayer's spouse, children, grandchildren, and parents, as well as colleagues), the transfer is taxable. The

Proposed 1061 Regulations broadly defined "transfer" in this context to include non-recognition transactions such as gifts or contributions to partnerships. As a result, under the Proposed 1061 Regulations, the gift of a profits interest would accelerate the transferor's gain.

The Final 1061 Regulations helpfully clarify that Section 1061(d) does not accelerate gain on a transfer and applies only to transfers where gain is recognized. Consequently, Section 1061(d) does not trigger the recognition of gain in otherwise tax-free transfers, such as contributions to partnerships or gift transfers that are often utilized in estate planning for fund managers. Nevertheless, any future realized gains in respect of such transferred APIs would remain subject to potential Section 1061 recharacterization.

Lookthrough rule for certain API dispositions

The Proposed 1061 Regulations treated the gain on the sale of an API as short-term capital gain in certain circumstances, even if the API had been held for more than three years. The relevant holding period for a sale of an API (or pass-through entity holding directly or indirectly an API) is generally tested by reference to the holding period in that entity. However, under the Proposed 1061 Regulations, if gain with respect to "substantially all" (80% or more) of the entity's assets would be recharacterized as short-term under Section 1061 if disposed of (due to a holding period of three years or less), then gain on the sale of such API would be recharacterized as short-term even if the seller of the API had satisfied the three-year holding period generally required by Section 1061.

Under the Final 1061 Regulations, the Lookthrough Rule has been significantly pared back, and replaced with an anti-abuse rule that is applicable only where, at the time of disposition of an API held for more than three years, (1) the API would have a holding period of three years or less if the holding period of such API were determined by excluding any period before which third-party investors have capital commitments to the partnership, or (2) a transaction or series of transactions has taken place with a principal purpose of avoiding potential recharacterization gain under Section 1061(a).

Carry waivers

In the Preamble to the Proposed 1061 Regulations, the IRS and the Treasury indicated they were aware of arrangements employed by fund managers to waive allocations of gain from a fund that would be treated as short-term capital gain pursuant to Section 1061, in order to be allocated future gain that could satisfy Section 1061's three-year holding period. The Preamble to the Proposed 1061 Regulations included a warning that such arrangements may be subject to challenge on various grounds and should comply with generally applicable tax laws, including those that also apply to so-called "management fee waivers" (which we previously have discussed in a prior alert). The Final 1061 Regulations (including the Preamble), however, are completely silent on carry waiver arrangements. Nevertheless, careful planning should continue to be used when implementing such arrangements.

Effective dates

The Final 1061 Regulations generally apply to tax years beginning on or after the date the Final 1061 Regulations are published in the Federal Register, and will therefore apply to taxpayers with a calendar tax year beginning January 1, 2022. Taxpayers are allowed to apply the Final 1061 Regulations prior to that date if they are applied consistently. Consistent with the Proposed 1061 Regulations, the rules for partnership interests held by S corporations are effective for tax years beginning after December 31, 2017 (the effective date of Section 1061), and the rules for partnership interests held by PFICs that have made a QEF election are effective for tax years beginning after August 14, 2020.

Potential for further changes

The Preamble to the Final 1061 Regulations foreshadows that additional Section 1061 guidance could be released. The IRS flagged several topics as remaining under study and solicited additional comments in

those areas. In particular, the impact of Section 1061 on the taxation of enterprise value for sales of partnership interests and management contracts remains under IRS study.

For a more detailed summary and analysis of the Final 1061 Regulations, please refer to our blog post.

IRS Offers Guidance on Acceptable E-Signatures and Extends Acceptance of E-Signatures Until 2023

In August 2020, as part of its response to the COVID-19 pandemic, the IRS stated in news release IR-2020-194 that it would begin permitting taxpayers to use electronic signatures on certain forms. The Service announced in a revised memorandum issued on April 15, 2021 (NHQ-01-0421-0001) that it would be extending the use of digital signatures until the end of 2021. In September 2021, the IRS released a fact sheet clarifying what constitutes an acceptable method of providing an electronic signature. According to the IRS fact sheet, authorized methods include:

1. A typed name on a signature block
2. A scanned or digitized image of a handwritten signature that's attached to an electronic record
3. A handwritten signature input onto an electronic signature pad
4. A handwritten signature, mark, or command input on a display screen with a stylus device
5. A signature created by a third-party software

The fact sheet also notes that the IRS will accept images of signatures on file types such as jpg, pdf, and tiff, among others. E-signatures may be used on a number of paper forms listed on the guidance. On November 18, 2021, the IRS released memorandum NHQ-10-1121-0005, which provides an updated list of forms for which it will accept electronic signatures.

Also released on November 18 was memorandum (NHQ-01-1121-0004) updating the one released in April. In the memo, the revised memorandum extends IRS acceptance of electronic signatures on certain forms to October 31, 2023. The guidance applies to forms signed and postmarked on or after August 28, 2020. Please refer to the revised memorandum for a complete list of relevant forms.

New York and California Enact SALT Workarounds

Since the Tax Cuts and Jobs Act of 2017 ("TCJA") capped state and local tax deductions at $10,000, several states have sought to circumvent the deduction limitation. In 2020, a number of states enacted workarounds in the form of a tax assessed on pass-through entities, some states making the tax elective and others like Connecticut making the tax mandatory. This pass-through entity tax (the "PTET") was accompanied by a corresponding state tax credit and aimed to benefit taxpayers by mitigating the impact of the $10,000 limit. Although the IRS and Treasury Department had rejected certain workaround attempts by states in the past, the IRS effectively permitted such entity-level tax workarounds in Notice 2020-75, issued on November 9, 2020.

In April 2021, New York passed the 2021/2022 budget bill, which included a PTET provision modeled after the guidance in Notice 2020-75. It allows partnerships and New York State S corporations to elect to pay PTET and receive an offsetting individual income tax credit. The annual deadline to elect into the tax workaround will be March 15 of the year for which the taxpayer wants the election to apply (the deadline for the 2021 PTET election was October 15, but it was an exception made just for this year). Once an election is made, it is irrevocable for that tax year. An entity opting into the PTET must pay it in four equal installments throughout the calendar year prior to the due date of the return (quarterly on March 15, June 15, September 15, and December 15).

California signed into law a similar workaround on July 16, 2021.

The Act has introduced plans to raise the state and local tax deduction cap from $10,000 to $80,000, to be applied from 2021 to 2030, and to revert to $10,000 in 2031.

The Ultra-Millionaire Tax Act of 2021

In the earlier part of 2021, Democratic Senators Elizabeth Warren and Bernie Sanders proposed a 3% wealth tax on individuals with a net worth exceeding $1 billion and a 2% tax on those with a net worth between $50 million and $1 billion.

Net worth would be composed of the value of all property owned by the taxpayer, excluding property valued at $50,000 or less, tangible personal property, and collectibles. Total net worth would be reduced by any debts owed by the individual.

The proposal has inspired a lot of debate. Many critics claim that a federal wealth tax would be unconstitutional, violating two provisions in the Constitution requiring that direct taxes by the federal government be apportioned among the states. Senator Warren, however, has the backing of a small group of scholars who argue that a wealth tax could be constitutional. Still, others are concerned about the administrative problems in implementing a wealth tax and the uncertain economic impacts of such tax.

More recently in October 2021, Senator Wyden proposed legislation that would institute a "Billionaires Income Tax" targeting the tradable assets of individuals that have more than $1 billion in assets or an adjusted gross income greater than $100 million for three consecutive years. The individuals targeted by the bill would be taxed on unrealized gains in their tradable assets on a yearly basis. Although the tax is not explicitly a wealth tax, many argue that it is a wealth tax in substance. Wyden's bill, like Senator Warren's proposal, has faced a fair bit of criticism, and there are doubts as to whether the bill would pass constitutional muster.

American Rescue Plan Act (ARPA) Phase 5 Stimulus Package

As a part of the federal government's response to the COVID-19 pandemic, Congress passed the American Rescue Plan Act (ARPA) earlier this year, bringing about relief to individuals, businesses, non-profits, and state/local governments. In addition to expanding the employee retention credit in Section 3134 and repealing the worldwide interest allocation election encoded in Section 864(f), the Act affected business loss deductions. Under Section 461(l), business losses that exceed the gross income of a non-corporate taxpayer by $250,000 (or $500,000 if on a joint return) are limited.

The IRS Concludes That Section 1031 Does Not Apply to Exchanges of Certain Cryptocurrencies

One June 18, 2021, the IRS released Memorandum 202124008, which addressed whether trades of certain cryptocurrencies that occurred prior to the TCJA could qualify as like-kind exchanges under Section 1031. The IRS memorandum examined this question in the context of three cryptocurrencies: Bitcoin, Ether, and Litecoin. In differentiating Bitcoin and Ether from Litecoin, the Service looked to their positions in the cryptocurrency market. Bitcoin and Ether differed from each other due to design and the way in which each was used.

The IRS ultimately concluded that cryptocurrency swaps involving Bitcoin, Ether, and Litecoin could not qualify as Section 1031 like-kind exchanges. Although the IRS in its Memo referred specifically to the three cryptocurrencies, the reasoning employed in its analysis (in some ways similar to the reasoning used in Rev. Rul. 82-166, in which it explained why gold bullion and silver bullion were not like-kind property) likely can be broadened to trades between other cryptocurrencies in the market.

Because the TCJA limited the applicability of 1031 like-kind exchanges to those transactions involving real estate, this Memo only has direct application to cryptocurrency exchanges taking place prior to

January 1, 2018. However, crypto transactions remain a focus of the IRS, so this guidance may provide background on the reasoning the IRS could apply when differentiating cryptocurrencies.

The Infrastructure Bill Introduces New Cryptocurrency Reporting Requirements and Premature Termination of the Employee Retention Tax Credit (ERTC)

President Biden signed the Infrastructure Investment and Jobs Act (the "Infrastructure Bill") into law on November 15, 2021. Included in the legislation are new cryptocurrency reporting rules, which in part, would require that a broker, defined as a person who facilitates transfers of digital assets on behalf of others, to report transactions involving cryptocurrencies on a Form 1099. Many "crypto" users worry that the term "broker" is defined too broadly and the rule may apply to those who are not equipped to deal with the reporting requirements, such as crypto miners, developers, and ordinary users.

The Infrastructure Bill, moreover, amends Section 6050I to require those receiving more than $10,000 worth of digital assets to file a Form 8300, Report of Cash Payments Over $10,000. Under this rule, those receiving the assets must include in their report the sender's personal information. Some argue this requirement may be burdensome if not impossible, as the information of transacting parties in a crypto environment are typically left anonymous. The new rules will be effective beginning January 1, 2023, meaning reporting will not begin until the following year in 2024.

The Infrastructure Bill also terminated the ERTC early. The ERTC was enacted in March 2020 as a part of the Coronavirus Aid, Relief and Economic Security Act (the "CARES Act") as a way to incentivize businesses to maintain their payrolls. The ERTC was originally scheduled to expire at the end of 2021, but under the Infrastructure Bill, it expires early, meaning that wages paid on and after October 1, 2021 are not eligible for the credit (there is, however, an exception for certain recovery startups).

Annual U.S. Tax Elections and Filings

This section briefly summarizes certain U.S. tax filings and elections (and related deadlines) relevant to private funds, their investors, and related persons.

Form 8832 Filings. If an entity filed an IRS Form 8832 (an entity classification election) with respect to 2021, that entity must attach a copy of the Form 8832 with its U.S. federal income tax return. If that entity is not required to file a U.S. return, all direct or indirect owners of that entity generally must attach a copy with their U.S. federal income tax returns if they are otherwise required to file U.S. returns. The deadline will be the due date (including any applicable extensions) of the filer's 2021 U.S. federal income tax return.

Form 1065. All U.S. partnerships must file a Form 1065, including limited liability companies (LLCs) classified as a partnership. The deadline is typically March 15.

"Qualified Electing Fund" (QEF) Election. If a private fund has invested in a non-U.S. portfolio company that is (or may be) a "passive foreign investment company" (PFIC), the first U.S. person in the PFIC's ownership chain (*e.g.*, the fund itself if a U.S. fund, or each U.S. investor if a non-U.S. fund) may wish to file a QEF election with respect to that PFIC. The QEF election must be filed with that U.S. person's U.S. federal income tax return for the first year in which the fund invested in the PFIC. The deadline for PFICs acquired in 2021 will be the due date (including any applicable extensions) of that U.S. person's 2021 U.S. federal income tax return.

"Electing Investment Partnership" (EIP) Election. Private funds that satisfy certain requirements may opt out of otherwise mandatory tax basis adjustments (including those that may result from transfers of interests in a fund) by filing an EIP election. The EIP election must be filed with the private fund's U.S. federal income tax return for the first year in which the election is intended to apply. For funds wishing to

be treated as EIPs with respect to 2021 (and subsequent years), the deadline will be the due date (including any applicable extensions) of the private fund's 2020 U.S. federal income tax return.

CbCR Reporting. A U.S. tax resident parent entity of a multinational enterprise (MNE) group that has revenues of $850 million or more during the taxable year must file IRS Form 8975 by the due date (including any applicable extensions) of its 2020 U.S. federal income tax return.

Certain U.S. Tax Filings with respect to Non-U.S. Entities. U.S. private funds and their U.S. investors may be required to make certain filings with respect to non-U.S. entities owned by the private fund. These filings may include, without limitation:

- IRS Form 5471 (with respect to certain non-U.S. corporations, including "controlled foreign corporations," owned by the private fund);
- IRS Form 926 (with respect to certain contributions of property to a non-U.S. corporation);
- IRS Form 8621 (with respect to certain non-U.S. corporations that are PFICs; however, such reporting generally is not required of U.S. tax-exempt investors);
- IRS Form 8865 (with respect to certain non-U.S. partnerships);
- IRS Form 8858 (with respect to certain non-U.S. disregarded entities);
- IRS Form 8938 (with respect to certain non-U.S. financial assets); and
- IRS Form 8992 (with respect to certain U.S. shareholders of controlled foreign corporations to calculate their share of "global intangible low-taxed income" (GILTI)). Generally, the deadline will be the due date (including any applicable extensions) of the U.S. person's 2021 U.S. federal income tax return.

ERISA

DOL's Latest ESG Proposal: The More Things Change, the More They Stay the Same

On October 14, 2021, the U.S. Department of Labor's Employee Benefits Security Administration (DOL) published in the *Federal Register* a new proposed regulation (Proposed Rules) on fiduciary responsibility in selecting ERISA plan investments and exercising shareholder rights (proxy voting). The Proposed Rules reflect an effort to "warm" a "chilling effect" that existing regulations have had on considering ESG factors in investing plan assets, but they do not include major changes to core principles. Most notably, the Proposed Rules retain the rule that investment decisions and the exercise of shareholder rights must be based solely on risk and return factors *(i.e.*, one may not sacrifice investment returns or take additional risk in support of a collateral objective), and do not offer a "safe harbor" for adding an ESG-themed investment fund to a 401(k) or 403(b) plan lineup.

Key Takeaways:

- The Proposed Rules (if finalized) should provide ERISA fiduciaries with some much-needed clarity and comfort that they will not be penalized for appropriately considering ESG-type factors when weighing investment alternatives, where those factors are material to the risk-return analysis.

- Although the Proposed Rules would not provide carte blanche for a fiduciary to select investments solely based on ESG factors that are unrelated to the interests of participants and beneficiaries in retirement income or financial benefits — which would violate ERISA's statutory duties of investment prudence and loyalty in any event — they should eliminate some of the burdens and uncertainty surrounding ESG-related investment decisions under the current rule. They do not, however, go so far as to label ESG-themed funds or investments as a special or separate asset class, which means that there is no "safe harbor" for a fiduciary to simply add the "best" of a selection of ESG-themed funds to a 401(k) or 403(b) investment fund lineup.
- When making investments in private investment funds or hiring an investment manager, ERISA plan fiduciaries are likely to be more focused on the manager's ESG policies.
- Driven by a concern that the current rules have had the effect of chilling proxy voting activity by plan fiduciaries, the Proposed Rules would eliminate the existing burdensome proxy voting-related recordkeeping requirements and underscore that exercising shareholder rights (including proxy voting) is a key tool in managing plan investments that should be taken seriously by ERISA fiduciaries.

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Although the Proposed Rules (if finalized) would swing the pendulum back in the direction of permitting (as opposed to prohibiting) ERISA fiduciary consideration of ESG factors under certain circumstances, the bedrock principles of ERISA's fiduciary duties of prudence and loyalty as applied to investment decisions generally remain unchanged – in particular, ERISA plan fiduciaries will still generally be required to base their investment decisions solely on the risk-adjusted value to plan participants and beneficiaries and in a manner so as to not subordinate their economic interests (such as by sacrificing investment returns or taking on additional risk) to unrelated goals or objectives.

DOL Steps into the Cybersecurity Discussion

Formally wading into the cybersecurity discussion for the first time, on April 14, 2021, the DOL posted on its website a suite of new cybersecurity guidance which was aimed at ERISA plan service providers (Cybersecurity Program Best Practices), plan fiduciaries (Tips for Hiring a Service Provider with Strong Cybersecurity Practices) and plan participants and beneficiaries (Online Security Tips for Participants and Beneficiaries).

By way of background, cybersecurity has over the last decade become an area of critical importance to sponsors and administrators of employee benefit plans as well as plan participants. Put simply, this is because plans (which the DOL estimates hold $9.3 trillion in assets) are a prime target of cyber-thieves, given that they typically hold significant amounts of sensitive participant data, often permit electronic access to funds (think 401(k) distributions) and rely on outside service providers, who provide additional access points for breach. This risk was only exacerbated by the COVID-19 shutdowns, where benefits personnel and their service providers quickly had to transition to working remotely and began relying on electronic access more than ever before.

The Tips for Hiring a Service Provider with Strong Cybersecurity Practices document provides some succinct suggestions for steps that plan sponsors and administrators might take with respect to diligence of, and contracting with, plan service providers such as investment managers, custodians and brokers. The suggestions recommend that plan fiduciaries conduct very specific diligence into a potential service

provider's cybersecurity practices (and track record relating to cybersecurity) and negotiate specific contractual rights relating to ongoing compliance with cybersecurity and information security standards. When making investments in private investment funds or hiring an investment manager, ERISA plan fiduciaries are more likely to be focused on these issues.

For more information, please see here.

Employment Law

Harassment, Discrimination and Pay Equity

Connecticut

Connecticut Governor Ned Lamont signed into law An Act Deterring Age Discrimination in Employment Applications (DAD Act), which prohibits employers, or employers' agents, from requesting or requiring applicants to provide their age, date of birth, or dates of attendance at, or date of graduation from, an educational institution on an initial employment application. Effective October 1, 2021, the DAD Act applies to all employers with three or more employees. It amends Connecticut's Fair Employment Practices Act (CFEPA) by making it a discriminatory practice for an employer to request or require the above-mentioned information, subject to two exceptions: the prohibition does not apply to an employer requesting or requiring such information (i) based on a bona fide occupational qualification or need; or (ii) when such information is required to comply with any provision of state or federal law. An aggrieved applicant may file a complaint alleging violation of the Act with the Connecticut Commission on Human Rights and Opportunities.

Connecticut also enacted An Act Creating a Respectful and Open World for Natural Hair, which amends CFEPA to define race as "inclusive of ethnic traits historically associated with race, including, but not limited to, hair texture and protective hairstyles." The new law further defines "protective hairstyles" as including, but not limited to, "wigs, headwraps and hairstyles such as individual braids, cornrows, locs, twists, Bantu knots, afros and afro puffs." The law took effect immediately upon signing in March 2021. Connecticut has joined the growing list of states that prohibit discrimination on the basis of traits historically associated with race, including hair, including California, Colorado, Maryland, New Jersey, New York, Virginia, and Washington

Virginia

Virginia amended the Virginia Human Rights Act (VHRA) to include additional employment protections for individuals with disabilities. The amendments bring the Virginia anti-discrimination protections in line with those provided by the federal Americans with Disabilities Act and also creates new reasonable accommodation requirements. The new law requires employers to provide reasonable accommodations necessary to assist otherwise qualified disabled persons to perform their job. Employers must also engage in good faith in the interactive process when an employee requests a reasonable accommodation.

Like the ADA, the law contains an "undue burden" exception for the obligation to provide reasonable accommodations. To avail itself of the exception, the employer must demonstrate the accommodation would impose undue hardship on the employer, assessed by considerations such as:

- Hardship on the conduct of the employer's business, considering the nature of the employer's operation, including composition and structure of the employer's workforce;
- Size of the facility where employment occurs;
- The nature and cost of the accommodations needed, taking into account alternative sources of funding or technical assistance;
- The possibility that the same accommodations may be used by other prospective employees; and
- Safety and health considerations of the person with a disability, other employees, and the public.

Virginia employers are required to include information on employees' rights to reasonable accommodations for disabilities in their employee handbook and post the same in a "conspicuous" place at the location of employment. Lastly, employers cannot take an adverse action against an employee because they request or use a reasonable accommodation. Please see our blog post from June 24, 2021 for more information.

Illinois

Illinois amended the Illinois Human Rights Act to prohibit employers from using an individual's conviction record as a basis to refuse to hire, segregate or act with respect to the recruitment, hiring, promotion, discharge or other term and condition of employment. There is an exception, however, if there is a "substantial relationship" between one or more of the previous criminal offenses and the employment sought or held. An employer may also consider an individual's conviction record if the granting or continuation of employment would involve an "unreasonable risk" to property or to the safety or welfare of specific individuals or the general public.

A "substantial relationship" exists if employers must consider whether the employment position offers the opportunity for the same or a similar offense to occur and whether the circumstances underlying the conviction will recur in the employment. Employers must also consider a number of mitigating factors, including the length of time since conviction, the severity of the conviction and evidence of rehabilitation efforts. If, after considering the mitigating factors, the employer makes a preliminary decision that the individual's conviction record is disqualifying, the employer is required to notify the employee of its preliminary decision in writing. Please see our blog post from March 24, 2021 for more information

Illinois also amended the Illinois Equal Pay Act ("IEPA") to require private businesses with more than 100 employees to obtain an "equal pay registration certificate" by March 23, 2024 and every two years thereafter. To apply for the certificate, a business must submit an equal pay compliance certificate, a copy of the employer's most recent EEO-1 report and report the total wages paid to each employee during the previous calendar year. The certification certifies that:

- The business is in compliance with Illinois and federal equal pay laws;
- The business is in compliance with Title VII of the Civil Rights Act of 1964, the Equal Pay Act of 1963, the IHRA, the Equal Wage Act and the IEPA;
- The average compensation for its female and minority employees is not consistently below the average compensation for its male and non-minority employees within each of the major job categories in the Employer's EEO-1 report, taking into account factors such as length of

service, requirements of specific jobs, experience, skill set, effort, responsibility, working conditions of the job, or other mitigating factors;

- The business does not restrict employees of one sex to certain job classifications and makes retention and promotion decisions without regard to sex;
- Wage and benefit disparities are corrected when identified to ensure compliance with the laws referenced above; and
- Wages and benefits are evaluated to ensure compliance with the laws referenced above, as well as the frequency of any such evaluations.

The employer must also disclose on its equal pay compliance statement how it establishes compensation and benefits (*e.g.*, a market pricing approach, state prevailing wage or union contract requirements, etc.)

If the business does not obtain an equal pay registration certification, the Illinois Dept. of Labor can impose a penalty in an amount equal to 1% of the business's gross profits. Please see our blog post from March 24, 2021 for more information.

Texas

Texas Governor Greg Abbott signed two new bills into law, effective September 1, 2021, that increase legal protections against sexual harassment. The first bill (House Bill 21) lengthens the statute of limitations applicable to sexual harassment claims under state law. Currently, employees must file a charge of discrimination with the Texas Workforce Commission within 180 days of the alleged harassing conduct. Under the new law, the statute of limitations for filing sexual harassment claims will increase to 300 days from the date of the alleged harassment. The longer limitations period applies only to sexual harassment claims based on conduct that occurs on or after September 1, 2021. The current 180 day statute of limitations remains unchanged for other types of alleged discrimination. The second bill (Senate Bill 45) expands the definition of employer for purposes of sexual harassment claims. Currently, only employers with 15 or more employees can be liable for sexual harassment under Texas law. The new law adds Section 21.141 to the Texas Labor Code, which applies specifically to sexual harassment claims and defines "employer" to include anyone "who: (i) employs one or more employees; or (ii) acts directly in the interest of an employer in relation to an employee)". Like House Bill 21, the newly-expanded definition of "employer" provided by Section 21.141 does not apply to other forms of alleged discrimination or harassment. Senate Bill 45 also imposes a heightened duty on employers to remedy sexual harassment. Currently, employers may be liable for sexual harassment committed by a coworker if the employer knew or should have known of the harassment and failed to take adequate remedial action. Under newly-added Section 21.141 of the Texas Labor Code, an employer commits an unlawful employment practice if "sexual harassment of an employee occurs and the employer or employer's agents or supervisors: (1) know or should have known that the conduct constituting sexual harassment was occurring; and (2) fail to take immediate and appropriate corrective action." The law does not further define "immediate and appropriate corrective action."

Safe and Sick Leave Laws

Chicago

On August 1, 2021, the City of Chicago amended its Minimum Wage and Paid Leave Ordinance (Ordinance) to include additional uses of paid leave for eligible employees. An employee who works at least 80 hours for an employer within any 120-day period while physically present within the geographic boundaries of Chicago may use sick leave for the following reasons:

- The employee is ill or injured, or for the purpose of receiving professional care, including preventive care, diagnosis, or treatment, for medical, mental, or behavioral issues, including substance-use disorders;
- A member of the employee's family is ill, injured, or ordered to quarantine, or to care for a family member receiving professional care, including preventive care, diagnosis, or treatment, for medical, mental, or behavioral issues, including substance-use disorders;
- The employee, or member of the employee's family is the victim of domestic violence or a sex offense;
- The employee's place of business is closed by order of a public official due to a public health emergency, or the covered employee needs to care for a family member whose school, class, or place of care has been closed; or
- An employee obeys an order issued by the Mayor, the Governor of Illinois, the Chicago Department of Public Health, or a treating healthcare provider, requiring the employee to: (i) stay at home to minimize the transmission of a communicable disease; (ii) remain at home while experiencing symptoms or sick with a communicable disease; (iii) obey a quarantine order issued to the employee; or (iv) obey an isolation order issued to the employee.

Please see our blog post from August 10, 2021 for more information.

Wage and Hour

New York

New York enacted amendments, known as the "No Wage Theft Loophole Act," to Sections 193 and 198 of the New York Labor Law, to state "[t]here is no exception to liability [under those sections] for the unauthorized failure to pay wages, benefits, or wage supplements." The purpose of the amendment was to clarify that employees can bring § 193 claims not only for unauthorized "line-item" deductions from wages but also for the wholesale withholding of wages alleged to be owed. Practically, the amendments may allow a broader range of employees to assert statutory claims for the failure to pay compensation allegedly owed, including claims for bonus compensation or other incentive plans. Please see our blog post from September 19, 2021 for more information.

Family and Medical Leave Developments

Washington D.C.

Washington D.C. enacted significant changes to its paid medical, parental and family care law. Effective October 1, 2021 (with a minor exception for expanded personal medical leave) the Universal Paid Leave Emergency Amendment of Act of 2021 ("PLEAA") amends the D.C. Universal Paid Leave Amendment Act of 2016, as well as the D.C. Family and Medical Leave Act of 1990, and other provisions related to paid leave under the District's Paid Family Leave ("PFL") program, to expand benefits for covered individuals, including:

- Adding prenatal care and pregnancy loss coverage as qualifying reasons for leave; and
- Increasing the paid leave duration for individual personal medical needs to 6 weeks, up from the previous 2 workweeks. Starting in 2022, the maximum durations of paid leave available under the paid family leave program may be modified on an annual basis.

Please see our blog post from October 5, 2021 for more information.

Massachusetts

Massachusetts Paid Family and Medical Leave ("PFML") law went into effect on January 1, 2021. Under that law, qualified individuals may utilize:

- Up to 12 weeks of family leave per benefit year in order to:
  - (i) bond with a newborn child within the first 12 months after the child's birth;
  - (ii) bond with a child within the first 12 months after adoption or foster care placement; or
  - (iii) manage family affairs when a family member is on active duty in the armed forces.
- Up to 20 weeks of medical leave per benefit year when the employee is unable to work due to their own serious health condition.
- Up to 26 weeks to care for a covered service member with a serious health condition.

Additionally, starting July 1, 2021, qualified individuals may take up to 12 weeks of family leave per benefit year in order to care for a family member with a serious health condition. After the first 7 calendar days, qualified individuals will be paid a percentage of their salary or earnings. The maximum weekly benefit available to a qualified individual is $850/week. The maximum rate is to be recalculated each year. Please see our blog post from December 22, 2020 for more information.

COVID-19 Workplace Safety Measures

Several states, including New York, Virginia and Maryland have passed legislation requiring employers to adopt workplace safety standards in response to the COVID-19 pandemic. New York's requirements are discussed in greater detail below.

New York

In May 2021, New Yok passed the HERO Act, which requires all employers in New York to implement safety standards and adopt a plan to protect against the spread of airborne infectious diseases in the workplace. Employers are required to adopt the state model or implement their own written plan that meets or exceeds the standards set forth in the state model. The HERO Act requires employers with at least 10 employees to permit employees to form a "workplace safety committee" that would be authorized to, among other things, (i) raise health and safety concerns; (ii) review any policy put in place in the workplace required by the HERO Act and provide feedback; (iii) review the adoption of any policy in the workplace in response to any health or safety law, ordinance, rule, regulation, executive order, or other related directive; (iv) participate in any site visit by any governmental entity responsible for enforcing safety and health standards in a manner consistent with any provision of law. Employers may be required to pay penalties of $50 or more per day for not creating a plan and up to $10,000 for not following an adopted plan. The HERO Act also prohibits retaliation against employees who exercise their rights under the HERO Act, including raising questions about compliance with the safety and health plan. Please see our blog posts from April 21, 2021, September 23, 2021 and October 7, 2021 for more information.

Proskauer's "ProTrack COVID-19"

The COVID-19 crisis has presented employers with significant legal and compliance challenges over the last 19 months. Federal, state and local legislatures have passed and amended laws and regulations on a near-constant basis. To assist multi-state employers as they navigate these developments, Proskauer has developed ProTrack COVID-19, a state and local law tracker tool. Our proprietary tracker allows employers to search the legal requirements in the jurisdictions where they conduct business, and provides realtime updates. Please click here for information regarding Proskauer's ProTrack COVID-19 platform.

Non-Competition Agreements and Restrictive Covenants

Washington D.C.

In December 2020, the Council of the District of Columbia passed the "Ban on Non Competes Agreements Amendment Act" (Ban Act). The Ban Act, with limited exceptions, will make non-competes entered into after the effective date of the law void and unenforceable. At the moment, the effective date has been deferred to at least April 2022. The Ban Act also prohibits employers from maintaining workplace policies that prevent employees from working for other employers and retaliating against employees for exercising their rights under the Ban Act. The Ban Act imposes a near-total ban on non-compete agreements in D.C., prohibiting employers from barring any employee, excluding babysitters, religious organization workers, volunteers and certain medical professionals from working for competitors not only after their employment ends, but also during their employment. The Ban Act also includes both administrative and civil penalties to deal with employer non-compliance. Please see our blog posts from December 18, 2020, May 26, 2021 and July 16, 2021 for more information.

Illinois

Illinois amended the Illinois Freedom to Work Act (IFWA), which imposes restrictions on the use of non-competition and non-solicitation (employee and customer) restrictive covenants for Illinois employees. The law takes effect on January 1, 2022, and only applies to restrictive covenants entered into after January 1, 2022.

Key provisions of the law include:

- The law prohibits employers from entering into non-competition agreements with employees who earn $75,000 per year or less and also prohibits employers from entering into non-solicit agreements with employees who earn $45,000 per year or less.
- For non-compete agreements, the salary threshold amounts will increase every five years by $5,000 until January 1, 2037, when the amount will equal $90,000. For non-solicit agreements, the salary threshold amounts will increase every five years by $2,500 until January 1, 2037, when the amount will equal $52,500.
- Employers must advise employees to consult with an attorney before entering into a non-compete or non-solicit agreement and must also provide employees at least 14 days to review the agreement and decide whether to sign. Employees have the option of signing the agreement before the 14-day period has ended.

Please see our blog post from August 19, 2021 for more information.

Cannabis and Employment

New York

On March 31, 2021, New York enacted the Cannabis/Marijuana Regulation & Taxation Act (MRTA), which legalized the use of recreational marijuana for individuals 21 and older. Significantly for employers, MRTA makes clear that it is not intended to limit an employer's ability to prohibit cannabis use in the workplace. However, MRTA amends section 201-d of the New York Labor Law, which prohibits discrimination because of an individual's lawful outside work activities, to include cannabis use in accordance with state law. The law does provide employers a few narrow exceptions including:

- the employer's actions were required by state or federal statute, regulation, ordinance, or other state or federal government mandate;
- the employee is impaired by the use of cannabis, meaning the employee manifests specific articulable symptoms while working that decrease or lessen the employee's performance of the duties or tasks of the employee's job position, or such specific articulable symptoms interfere with an employer's obligation to provide a safe and healthy workplace, free from recognized hazards, as required by state and federal occupational safety and health law; or
- the employer's actions would require such employer to commit any act that would cause the employer to be in violation of federal law or would result in the loss of a federal contract or federal funding.

Employers are not permitted to test employees for cannabis unless one of the above exceptions apply. Employers may also prohibit employees from possessing cannabis at the worksite or otherwise on the employer's property, including in company vehicles, rented space, and areas used by employees on company property.

Please see our blogs posts from March 31, 2021 and October 27, 2021 for more information.

Non-Disclosure and Confidential Settlement Agreements

California

Currently, California Civil Procedure Code section 1001 (Section 1001) prohibits settlement agreement provisions that bar disclosure of factual information regarding an administrative or civil claim for sexual assault, sexual harassment, harassment or discrimination based on sex, failure to prevent such an act, or retaliation against a person for reporting such an act. For purposes of agreements entered into on or after January 1, 2022, the new bill expands the prohibition to include acts of workplace harassment or discrimination **not** based on sex. Consistent with existing law, a provision that shields the identity of the claimant and facts that could lead to the discovery of the claimant's identity, including pleadings filed in court, may be included within a settlement agreement *only at the request of the claimant*. Additionally, the law permits the entry or enforcement of a provision in any agreement that precludes the disclosure of the amount paid in settlement of a claim. And the bill does not limit the ability of parties to agree to complete confidentiality in settlements of threatened claims that have not been filed before an administrative agency or court.

Further, under the California Fair Employment and Housing Act, it is currently an unlawful employment practice for an employer, in exchange for a raise or bonus, or as a condition of employment or continued employment, to require an employee to sign a non-disparagement agreement or other document that

purports to deny the employee the right to disclose information about "unlawful acts in the workplace," including, but not limited to, sexual harassment or discrimination. After January 1, 2022, "unlawful acts in the workplace" is expanded to include any form of harassment or discrimination. Further, if an employer requires employees to sign a non-disclosure agreement during employment, the new law requires that employers include the following language: "Nothing in this agreement prevents you from discussing or disclosing information about unlawful acts in the workplace, such as harassment or discrimination or any other conduct that you have reason to believe is unlawful."

Please see our blog post from October 18, 2021 for more information.

New York

The New York State Division of Human Rights (NYS Division) issued a notice, partially reproduced on the NYS Division's website, announcing a significant change in policy regarding the agency's processes for complaint resolution: since October 13, 2021, the NYS Division no longer grants requests for discontinuance of complaints due to confidential private settlements. As stated in the NYS Division's notice, if a complainant seeks to discontinue an action prior to a hearing, the complainant's attorney will be required to state in writing why the discontinuance is sought and if the reason is private settlement, the discontinuance will not be granted. Instead, the parties will be permitted to either settle the matter publicly through an Order after stipulation that includes the terms of the settlement, or proceed through the NYS Division's public hearing process. The Division states that this is "in the public interest for transparency and good governance." The NYS Division's notice further states that it will no longer issue Commissioner's Orders simply discontinuing complaints after a private settlement, but will instead require public disclosure of settlement terms, through either an Order or a public hearing.

Executive Compensation

Profits Interests vs. Phantom Carry

Compensation packages for fund managers typically include performance incentives that align their compensation with the fund's performance and the timing of distributions made by the fund. Traditional profits interests (carry) are often attractive, because they provide a way for compensation to be taxed at the capital gains rate rather than ordinary income rates. Also, profits interests can often be subject to forfeiture (or buy-back for an amount below fair market value) upon breach of a restrictive covenant; so profits interests can be used as a carrot to incentivize compliance with any such covenants. An important drawback, however, is that holders of profits interests generally have to be treated as partners, which means they need to get annual K-1s (even before they are vested) and cannot be treated as employees of the issuer.

"Phantom" carry arrangements are a way to mirror the economics of a profits interest, but without making employees into partners. There are two key drawbacks to a phantom carry arrangement. First, payments under the arrangement are treated as ordinary income that is subject to withholding for income and employment taxes (at rates that are higher than capital gains rates). Second, phantom carry arrangements are subject to Section 409A of the Internal Revenue Code (and, for some funds, Section 457A).[5] This means that phantom carry arrangements typically must specify a payment schedule that is

[5] In general, Section 457A applies to (1) foreign corporations with respect to which significant income is not subject to tax in the U.S. or under a comprehensive foreign income tax regime, and (2) partnerships for which significant income is allocated to tax-exempt entities or to foreign persons who are not subject to income tax in the U.S. or under a comprehensive foreign income tax regime. For example, most offshore funds are subject to Section 457A.

not aligned with the timing of distributions made by the fund pursuant to the LLC or partnership agreement. Failure to comply with these payment schedules would result in accelerated income tax on the full value of the award (before the recipient is paid and before there is an underlying distribution by the fund to generate cash) plus an additional 20% tax. The taxes fall on the employee, but the employer also has a reporting obligation, each of which create additional risk.

In general, there are two ways to structure a phantom carry arrangement to delay income tax until the time of payment and to avoid the 20% additional tax:

(i) Condition payment on the employee remaining employed until shortly before the payment is made. This approach is useful for retention, but can cause problems if the fund has a long investment horizon and it does not provide the executive with any "vested" interest if he or she resigns or terminates employment involuntarily.

(ii) Specify a payment schedule that complies with the requirements of Section 409A. (This approach is not available if the fund is subject to Section 457A.) To comply with Section 409A, the arrangement must specify in advance that payment will be made upon a specified event (separation from service, death, disability, financial hardship, or a change in control) or at a specified time (or times). Structuring payments around a Section 409A-compliant payment schedule is complicated and requires the assistance of counsel well-versed in the Section 409A traps.

The Mobile Workforce and Related Complexities

The COVID-19 pandemic has helped usher in a host of changes to the work environment. Principally, "working from home" or "remotely" is a feature of work environments that looks to be here to stay. As a result, employees have more opportunities than before; they do not need to move to take a new job and they can move without having to change jobs. A positive for employers is greater access to talent--not just those individuals who are located near a specific office of the company. But, how do you retain employees when opportunities abound? Employers have both "carrots" and "sticks" in their toolbox to overcome this challenge.

Recently, we have seen an uptick in retention bonuses being offered. These bonuses can be designed to pay out solely based on continued employment or include performance conditions as well. Similarly, existing compensation programs can be designed to reward both specific company goals as well as "soft" goals that seek to develop a strong company culture. For example, there has been increased prevalence of performance metrics tied to environmental, social and governance issues affecting a company's business. On the flip side, employers could potentially use restrictive covenant agreements (i.e., non-competition and non-solicit of customer and employee clauses) to restrict employee movement and reduce turnover. These are not perfect solutions. For example, many states already restrict the use of restrictive covenant agreements and other states are seeking to pass laws to restrict their use.

In addition to retention issues that are raised as a result of a more mobile workforce, "remote" work raises other complexities, including:

(i) Employee withholding may be impacted. Every state where an employee lives or works has a right to tax the employee's income. This means that employers can have obligations in states where they previously did not do business.

(ii) For non-exempt employees, it may be more difficult to track hours worked and meal breaks.

(iii) Employers need to manage providing tools for remote work. For example, laptop computers and phones are obvious, but things like ergonomic support, paper, and ink can be more complicated. Some state laws impose minimum requirements.

(iv) Employees located in jurisdictions where the employer did not previously have employees may also implicate other state laws and regulatory issues. For example, the mere presence of employees in a specific state could potentially create state sales tax requirements or the requirement to register the company to do business in that state.

Shareholder Activism

SEC to Tighten Rule 10b5-1 Trading Plan Rules

The SEC is expected in the near future to propose amendments to its rule permitting advance trading plans that would place restrictions, or "speed bumps," on how funds implement trading plans, although the SEC is not expected to limit the scope of persons who are entitled to use the plans. This initiative is motivated by increasing criticism of the rule over the last few years, coupled with studies highlighting a concern that insiders using trading plans have the ability to time their stock sales more successfully compared to other market participants.

This initiative is a front-burner item for the SEC and for its legislative overseers, as reflected by statements by Chairman Gensler, proposed legislation in Congress, and focus by the SEC's Investor Advisory Committee (IAC), which has published a draft report. The amendment proposals could be coupled with more active SEC enforcement activity.

The Current Rule and Market Practice

Under the current rule, funds seeking to sell equity in portfolio companies sometimes use advance trading plans, or "10b5-1 plans" based on the safe harbor provided by Rule 10b5-1 under the Exchange Act. Under that rule, a fund may adopt an advance trading plan with its broker during a company's open trading window period that will permit trading to continue even after the window period ends. This approach may be helpful, for example, when the fund that wishes to sell down its position by sales in the open markets cannot complete a sufficient volume of trades during window periods, due to limitations posed by daily trading volumes and/or market volatility.

There is currently no substantive limit on the number of ways that a trading plan may be formulated, so long as the fund does not have MNPI when the plan is adopted, does not have input into or influence over trading once the plan is set in motion, and does not enter into a hedging or opposite-way transaction that has the effect of neutralizing the effect of the plan. A typical approach is where the fund provides its broker with discretion to sell fixed numbers of shares at different price levels. More rarely, funds use 10b5-1 plans to implement distributions outside of trading window periods.

Although few limitations are imposed by the current rule, there are practice guidelines based on statements by the SEC and its staff, and/or market practice, and some of these guidelines are built into the fund manager's insider trading policies. These include the following:

- Amendments or terminations are discouraged, and generally advisable to limit to circumstances where there is an objective, legitimate basis for doing so (*e.g.*, the plan is irretrievably under water);

- Plans should ideally be six months or longer in duration, with a few exceptions, such as quarterly corporate buy-back plans; and

- There should be a “cooling off” period, such as 30 or 60 days, before sales commence under a plan to help support the fact that the person entering into the plan did not have MNPI.

SEC Proposals to Tighten the Rule

Although the SEC has not yet published formal proposals, statements by Chairman Gensler and the substance of the draft IAC report reflect that the following reforms are likely to be proposed:

1. A required “cooling-off” period, which the IAC proposes to be four months, far longer than current market practice. Thus far, it has not proposed a distinction between individual plans adopted by corporate insiders, on the one hand, and institutions and corporate plans, on the other. Current market practice is to have little or no cooling-off period for corporate transactions, and shorter periods for institutions, based on the theory that the need for “guardrails” less significant.

2. Limiting a single person or entity to one plan at a time, i.e., no multiple or overlapping plans.

3. Proxy statement disclosure of certain details of pending plans, as well as a prompt 8-K filing in the event of the adoption, amendment, or termination of a plan by the issuer or an affiliate, including executive officers.

4. Subjecting investors in “foreign private issuers” (including those filings ADRs and ADSs) to Section 16 reporting and possibly to short-swing liability, as they are currently exempt.

The SEC has a busy agenda with many competing priorities, but we would not be surprised to see proposals on this subject in 2022.

Insurance

During 2021, Proskauer continued to work with a wide variety of private investment funds of all types and sizes on insurance matters. This included representing fund clients in reviewing and negotiating their insurance programs, as well as recovering on their insurance claims through mediations, arbitrations and litigations. Below are a few of the key trends we saw in 2021 along with our thoughts on where we see things headed in 2022.

Challenging Underwriting Environment

After a decade-long favorable “soft” underwriting market, the market has hardened to an extent during 2020 and 2021. Many fund clients have seen increases in their premiums and/or retentions over the past two years. Unfortunately, some insurers have also attempted to use the current underwriting environment as an opportunity to seek to add unfavorable endorsements to policies that significantly restrict the coverage they provided in previous years. However, even in the current, more difficult underwriting environment, we have seen many examples of clients who have successfully negotiated to expand their current scope of coverage or find an alternative insurer when their current insurer was unwilling to continue providing the broad coverage it previously offered. Thus, the current underwriting market has made it all the more important for fund clients to carefully review and assess their coverage on each renewal.

Contentious Coverage Environment

During 2021, insurers in the fund space have taken aggressive positions in seeking to deny coverage, and we have represented a number of fund clients in coverage disputes with their insurers. We have seen insurers attempt to deny coverage on numerous grounds, including based on policy definitions,

policy exclusions, and public policy arguments. We have also seen many examples of insurers making the claim process difficult for their insureds, including refusing to provide consent to settlements, refusing to allow the insured to use its counsel of choice, and even denying coverage based on alleged breaches of policy consent and cooperation provisions. The aggressive positions taken by insurers in denying coverage and during the claim process reinforce the importance of carefully reviewing and negotiating coverage at the outset, as well as ensuring that the claim process is carefully navigated to avoid providing insurers with additional bases for seeking to deny coverage.

Evolving Cyber Insurance Market

The past year has been an interesting one in the cyber insurance market. On one hand, we have seen an increased interest in buying insurance coverage for cyber risks for a variety of reasons, including concern about such risks, requirements of investors or to satisfy regulators. On the other hand, the market for cyber insurance has hardened due to high-profile and costly cyber events, making it more difficult to purchase robust coverage. Careful analysis and review is necessary when obtaining insurance for cyber risks because it is rare for all cyber risks of concern to fund clients to be covered under the same policy. Instead, it is common for cyber "crime" risks (for example, social engineering and fraudulent transfers) to be covered under a crime policy or endorsement to a fidelity bond with other cyber risks (for example, data breaches and business interruption from cyber events) to be covered under a separate cyber policy. Coordinating these separate coverages is important to ensure that as broad a spectrum of cyber risks as possible are covered.

Attention to Protecting against Risks Arising from Portfolio Companies

Private equity firms and activist hedge funds continue to face risks from lawsuits against their individuals who serve as directors of portfolio companies and against the firm itself. During the past year, we have represented several clients in seeking insurance coverage for such lawsuits under both the funds' insurance policies and portfolio companies' policies. Coverage disputes in this scenario are both more likely and more difficult when attention has not previously been given to ensuring that the two sets of policies work together. Attention to capacity exclusions, allocation provisions, and outside capacity coverage agreements are critical. Careful review, negotiation and coordination of both sets of policies can help protect against the risks arising from portfolio companies to funds and individuals.

Focus on Protecting Individuals – Including When Serving In Outside Capacities

We have continued to see an increased focus on protecting individuals, as fund managers and boards continue to become savvier about the availability of insurance to protect against the legal and regulatory risks they face for managing investment funds and in serving in outside capacities, such as serving as directors for portfolio companies. This focus on individual protection has included review and negotiation of fund policies for protection of individuals in their respective capacities; review and negotiation of portfolio company policies; and an increased emphasis on obtaining dedicated insurance limits for individuals (called "Side A" policies") or for independent directors (called "IDL" policies) and to negotiate enhancements to such policies.

Coverage for SPACs

Purchasing insurance coverage for SPACs and their directors has become significantly more challenging during 2021. Due to increased concern about litigation risks related to SPACs, some insurers have exited the market for insuring SPACs while those that remain in the market have increased premiums, increased retentions and often begun adding exclusions that narrow coverage. There is also often significant pressure to get a policy placed on a time-sensitive basis, without any real review or negotiation, which

can lead to inadequate coverage being obtained. However, because of the significant litigation risks concerning SPACs, and the increasingly difficult insurance market, we have recently seen a substantial increase in fund clients seeking to more carefully review and negotiate coverage to ensure adequate protection for the SPAC entity and, critically, the individuals serving as directors. In light of the increasing costs of insurance for SPACs, we have also seen an increased interest in captive programs. When considering insurance for SPACs, it is also critical to ensure that the coverage for the SPAC is coordinated with the go-forward coverage for the new public company as well as other relevant insurance programs to ensure robust coverage for the entire SPAC and de-SPAC life cycle. The insurance market for SPACs will be an area of significant interest heading into 2022.

Attention to Coverage for Government Investigations

The risk of SEC and other government investigations continues to be a key concern for funds. Although many insurers' standard forms provide only limited coverage for investigations — as coverage is not triggered until late in the investigation (after significant costs had already been incurred) — if the policies are negotiated, most insurers will agree to provide coverage for the costs of defending government investigations from the very earliest stages. Given the wide availability and critical importance of this broad coverage, it is a significant missed opportunity for a fund manager not to seek and obtain such enhanced coverage.

Looking Ahead to 2022

There is a significant amount of debate in the broker and underwriting community as to whether the underwriting environment will soften in 2022. What appears much more certain, however, is that the challenging claim environment will continue into 2022. We therefore anticipate that there will be a number of new claim disputes in the funds space next year. Therefore, it will remain critical for fund clients to negotiate for as strong coverage as reasonably possible when purchasing or renewing coverage in order to minimize the chance of claims disputes and put themselves in a position of strength if a claim dispute does arise.

Reorganization and Chapter 11

Over the past year, important decisions have been rendered by federal courts (i) paving the way to the recovery of costs and expenses incurred by a stalking horse bidder related to a failed merger attempt with the debtor as administrative expenses in bankruptcy, and (ii) providing further guidance on determining whether a contract is "executory" in nature under Bankruptcy Code section 365.

Recovering Expenses Related to a Failed Merger as an Administrative Expense Claim

The Bankruptcy Code prioritizes payment of claims relating to the post-petition administration of the debtor estate—which, in many cases, receive payment in full. To receive such administrative expense priority, Bankruptcy Code section 503(b) generally requires that such claims be incurred in a post-petition transaction that yielded a "benefit to the estate." Common examples of administrative expenses include wages for the debtor's employees and fees for professionals assisting in the bankruptcy process.

When a debtor seeks to sell assets during its bankruptcy case, the presence of a stalking horse bidder provides many benefits, including setting the minimum price and other terms of the sale. To compensate a stalking horse bidder for the time and expense to perform the initial diligence and negotiation of a purchase agreement that forms the basis of competing bids, bankruptcy courts generally allow the debtor to provide certain protections to the stalking horse bidder. These bid protections can include

reimbursement of expenses incurred in connection with the transaction, and termination fees, among other things. However, when the sale to a stalking horse bidder fails to close, the ability to recover such fees and costs as an administrative expense is uncertain.

The *In re Energy Future Holdings* Decision

In *In re Energy Future Holdings Corp.*, 990 F.3d 728 (3d Cir. 2021), the U.S. Court of Appeals for the Third Circuit took a broad view of administrative expense treatment and opened up the path toward enhanced bid protections. The Third Circuit held that a stalking horse bidder could assert an administrative expense claim to recover costs and fees related to a failed merger attempt with the debtor, even if the bidder was not entitled to a termination fee pursuant to the terms of the merger agreement.

Energy Future Holdings (EFH) filed for bankruptcy in 2014. One of its most valuable assets was a majority indirect interest in Oncor Electric Delivery Company LLC (Oncor), the largest electric power distribution company in Texas. As a public utility company, Oncor is subject to state regulation through the Public Utility Commission of Texas (PUCT). In light of EFH's interest in Oncor, PUTC imposed certain restrictions on Oncor (a "ring fence")—requiring the creation of an "independent board with the sole right to determine dividends and placed restrictions on upstream distributions."

In 2016, EFH and NextEra Energy Inc. (NextEra) received court approval for a proposed merger, which was conditioned on the removal of the ring fence restrictions. After several attempts through negotiations and formal applications, the parties were unable to gain PUCT approval of a merger that did not include the ring fence restrictions. EFH eventually terminated the merger agreement with NextEra, and soon thereafter closed on a merger with another entity, which allowed for the ring fence to remain.

Following termination of the merger agreement and the bankruptcy court's denial of payment of the termination fee under the merger agreement, NextEra filed an administrative expense application for payment of its costs and expenses related to "its efforts to complete the transaction, obtain the requisite regulatory approvals, and complete the acquisition of Debtors' Oncor assets." NextEra argued that those actions benefited the estate by creating a "roadmap" for a future successful merger. The bankruptcy court dismissed the application, holding that the merger agreement barred the application, and in the alternative that the claim did not meet the requirements under the Bankruptcy Code.

After determining that the merger agreement did not prohibit NextEra from seeking an administrative expense claim, the Third Circuit held that NextEra made a plausible initial showing that its claim qualified as an administrative expense. First, the merger agreement fell within the definition of a post-petition transaction. Second, the court noted that analyzing the purported benefits of an action requires considering the costs of those actions to the estate as well. The court found merit in NextEra's argument that, through the merger negotiation process, NexEra "created guideposts that directly facilitated" the future successful merger. Therefore, NextEra "provided the estate with valuable knowledge and strategic documents that inured to the benefit of the Debtors." Court filings related to the subsequent merger showed that EFH used those resources to formulate a viable merger agreement with a subsequent entity. This benefit could outweigh the alleged costs stemming from NextEra's failed merger attempt. As a result, the Third Circuit reversed the bankruptcy court's dismissal of the administrative expense application and remanded the case to the bankruptcy court to make a factual determination as to whether NextEra provided a benefit to the estate.

Implications of the *In re Energy Future Holdings* Decision

Purchasing assets from a bankrupt estate, even after receiving court approval, includes the possibility of failure. Through its holding, the Third Circuit legitimized the argument that even a failed merger attempt can benefit the debtor estate and, therefore, fees and expenses incurred by a stalking horse bidder in the process could qualify for payment as an administrative expense, even when payment pursuant to the terms of the sale agreement is not an option. The success of this argument, however, will turn on the facts and circumstances surrounding the specific administrative expense application.

Third Circuit Provides Guidance on What Constitutes an "Executory" Contract

Bankruptcy Code section 365(a) provides a debtor the right to assume, assign, or reject "executory" contracts—*i.e.*, contracts where both parties have performance obligations remaining. Before a debtor can assume or assign an executory contract, the Bankruptcy Code requires the debtor to cure or provide adequate assurance that it will cure any defaults under the contract. However, the cure requirement does not apply to non-executory contracts. Thus, whether a contract will be considered "executory" in a bankruptcy proceeding should be a consideration when transacting with a distressed counterparty.

The *In re Weinstein Co. Holdings, LLC* Decision

The Third Circuit provided rare guidance into what constitutes an "executory" contract in *In re Weinstein Co. Holdings, LLC*, 997 F.3d 497 (3d Cir. 2021). In September of 2011, Bruce Cohen and his production company entered into a production agreement (Cohen Agreement) with a special purpose entity formed by The Weinstein Company (TWC) to produce the movie, *Silver Linings Playbook*. The agreement was structured as a "work-made-for-hire" contract which prevented Cohen's ownership of any of the film production's intellectual property. In turn, under the agreement, Cohen was provided $250,000 in fixed initial compensation as well as contingent future compensation equal to about 5% of the film's profits. The film was ultimately successfully produced in 2012.

However, in 2017, TWC's business plummeted following numerous sexual misconduct allegations against TWC's co-founder, Harvey Weinstein. In March 2018, TWC filed for Chapter 11 bankruptcy and sought bankruptcy court approval of a sale of its business to Spyglass Media Group, LLC (Spyglass). While the sale was approved and closed in July 2018, the purchase agreement provided Spyglass with the right to designate post-closing which of TWC's executory contracts it wanted to assume as part of the sale, and Spyglass agreed to pay any cure amounts necessary under the assumed executory contracts.

In October 2018, Spyglass sought a determination from the bankruptcy court that the Cohen Agreement was not executory, and therefore was transferred as part of the sale without the requirement to cure any defaults. If it was executory, Spyglass would have had to cure existing defaults and pay outstanding contingent compensation of approximately $400,000. However, if the Cohen Agreement was not executory, Spyglass was only liable on a go-forward basis following the closing of the sale.

In determining whether the Cohen Agreement was an "executory" contract, the Third Circuit examined whether the obligation of both Cohen and TWC was "so far unperformed that the failure of either to complete performance would constitute a material breach excusing performance of the other."

Under this test, the Third Circuit concluded that the Cohen Agreement was not executory. First, while TWC's obligation to pay contingent compensation to Cohen was "clearly material" because it far exceeded the payment of fixed compensation, Cohen's remaining obligations were mere "ancillary after-thoughts." The essence of the Cohen Agreement was for Cohen to produce the movie in exchange for money, which movie was released six years before TWC's bankruptcy. Cohen's remaining obligations

were to refrain from seeking injunctive relief about the movie, and indemnify TWC against third-party claims.

The Third Circuit rejected Cohen's argument that the parties had agreed that all of Cohen's obligations were material, because it was based on a strained reading of the Cohen Agreement. In doing so, however, the Third Circuit recognized that parties can override the Bankruptcy Code's intended protections for the debtor and a state's default contract rule regarding substantial performance. However, parties must do so by clear and unambiguous language.

Because the Cohen Agreement was not executory, it was transferred to Spyglass at the close of the sale, and Spyglass was not required to cure any defaults and pay Cohen the $400,000 outstanding contingent compensation under the agreement.

Implications of the *In re Weinstein Co. Holdings, LLC* Decision

This decision illustrates the importance of whether a contract will be considered "executory" in a bankruptcy proceeding when transacting with a distressed counterparty. Notably, at least in the Third Circuit, parties have the ability to specify "clearly and unambiguously" obligations that they intend to be material under an agreement, which could ultimately render the agreement executory.

European Union and United Kingdom

Brexit: UK withdrawal from the EU and the end of the Transitional Period

In March 2017, the United Kingdom (UK), formally notified the European Union ("EU") Council of the UK's intention to leave the EU under Article 50 of the EU's Lisbon Treaty. This triggered a two-year period during which the terms of the UK's exit from the EU were expected to be agreed. Whilst it was anticipated that the UK would leave the EU on 29 March 2019, this date was subsequently extended twice. On 31 January 2020 the UK formally left the EU (an event informally known as "Brexit") and entered into a transitional period until 31 December 2020 under which most EU legislation continued to apply in the UK in the same way as it did prior to Brexit. Prior to the end of the transitional period, the UK and the EU agreed and signed a free trade agreement (FTA). The UK subsequently left the EU Customs Union and Single Market on 31 December 2020 following the end of the transitional period agreed between the UK and EU and, on 1 January 2021, the FTA agreed between the UK and EU came into force.

Despite the FTA being agreed, there is still a great deal of uncertainty concerning many aspects of the UK's legal and economic relationship with the EU, including in relation to the provision of cross-border services. From a financial services perspective, the outcome is a 'hard' or no-deal Brexit scenario, as the FTA does not provide for a continuation of cross-border financial services. Accordingly, the UK firms which previously benefitted from the EU financial services "passport" (as detailed below) are no longer able to access this. However, this does not impact US fund managers in the same way as they do not have access to such "passports" and so would need to continue to market their funds *via* the national private placement regime (NPPR) of the relevant countries, where it is feasible to do so.

Impact of Brexit – Loss of the Financial Services Cross-Border "Passport" for the UK

From a financial services perspective, up until 31 December 2020 firms authorized in the UK were able to use an EU financial services "passport" under one or more EU Directives (such as the Markets in

Financial Instruments Directive (MiFID) or the Alternative Investment Fund Managers Directive (AIFMD)). This allowed such firms to carry out cross-border activities, whether through the provision of services or the establishment of a branch in other EU Member States. After the end of the transitional period, the UK became a "third country" (*i.e.*, a non-EU country) and the provisions applicable to third countries are now applicable to UK firms. This has resulted in a curtailment of the freedoms UK firms previously enjoyed. For example, UK alternative investment fund managers (AIFMs) are no longer able to use the cross-border marketing passport when marketing their alternative investment funds across the EU. Instead they need to market in other EU Member States by making NPPR notifications in each Member State into which they wish to market. It is possible that UK firms may be given a special status in future which would allow UK firms to continue to have access to the EU market on an "equivalent basis," but there is no clarity around this and this currently looks unlikely.

As the UK has retained the AIFMD regime as it is currently implemented into its domestic law for the foreseeable future, U.S. managers would continue to need to submit NPPR notifications to the UK Financial Conduct Authority (FCA) prior to marketing their funds in the UK. Any further future developments between the UK and the EU should be monitored closely and firms potentially impacted should be contingency planning on the potential longer-term effects of the UK leaving the EU.

New Rules Relating to the Pre-Marketing of Funds

On 2 August 2021, the EU legislative package (being made up of Directive (EU) 2019/1160 and Regulation (EU) 2019/1156) came into force; this aimed at reducing the regulatory barriers for the cross-border distribution of funds in the EU (CBDF Package). Specifically the CBDF Package was designed to address certain issues in the AIFMD and UCITS Directive relating to the marketing of funds under the AIFMD or UCITS marketing passports. Under the CBDF Package, there is a new harmonized definition of "pre-marketing" of funds whereas previously, the interlinked concepts of "pre-marketing" and "marketing" were interpreted differently between Member States. Under the CBDF rules, prior to any pre-marketing registration, managers will be able to only engage in high level discussions about the fund manager and its track record, with no reference to the relevant fund. Should a fund manager or its agents seek to provide specific information on the fund to investors in such EU Member States, then a prior pre-marketing registration for the marketing of the fund must be obtained from that Member State's regulator.

The new harmonized 'pre-marketing' definition in the CBDF Package allows for fund specific information, including draft PPMs or offering documents, to be provided to potential investors and for this to still fall within the scope of pre-marketing, as long as it does not amount to "an offer or placement" to an investor, which would trigger a formal marketing notification requirements.

Fund managers are required to send a notification to their local home state regulator within two weeks of beginning their pre-marketing. This notification will need to specify where and for which periods the pre-marketing is taking or has taken place, with a brief description of the pre-marketing (including information on the investment strategies presented and the AIF(s) covered). However, at the time of writing, not all EU Member States have implemented a form or process to make such notifications, meaning in certain jurisdictions (for example, Denmark), non-EU Mangers marketing under the NPPR will not be able to pre-market at all prior to the fund being formally approved under the NPPR.

Under the CBDF Package there is also a requirement for any third party carrying out pre-marketing on behalf of a fund manager to be authorized as an investment firm under MiFID, a CRD IV credit institution, a UCITS management company or an AIFM under AIFMD, or act as a tied agent in accordance with MiFID. In addition, the agent will be directly subject to the pre-marketing rules in the CBDF Package. Placement agents and fund distributors will need to make sure that they are in compliance with this new

requirement, which may involve having to set-up or engage an EU based firm with the appropriate authorizations.

Furthermore, the new regime attempts to provide further clarity regarding the use of "reverse solicitation" as a fundraising strategy. Any subscription by professional investors in the relevant EU Member State within 18 months of the EU AIFM having begun pre-marketing will be deemed to have taken place as a result of active "marketing" (triggering the requirement to make a formal marketing notification). However, it is unclear as to whether this would apply on a "per investor" or "per jurisdiction" basis. Should regulators interpret this on a "per jurisdiction" basis, this would mean that "marketing" and the associated requirements would be triggered upon any investor being pre-marketed to in that EU Member State. The approach and interpretation by the EU Member State regulators on this point is lightly to vary and so should be assessed on a Member State by Member State basis.

The CBDF Package also created new de-notification requirements, which include that EU AIFMs must notify their home Member State regulator when intending to cease marketing of an AIF. This would mean that the EU AIFM will not be able to carry out pre-marketing in relation to the AIF and a "similar investment strategy" or "investment ideas" for 36 months after the de-notification. There is no further guidance as to how these terms should be interpreted, but this could potentially be problematic should it extend to a restriction on pre-marketing further AIFs by a particular AIFM albeit that the default solution in such circumstances would be to not de-notify or not to make a pre-marketing notification at all and just make a full marketing notification.

The requirements of the CBDF package applies to EU AIFMS and a number of EU Member States have applied the requirements to non-EU AIFMs (including US managers) marketing funds under the NPPRs. When a non-EU AIFM seeks to raise capital in one or more EU Member State, it should be assessed to what extent that Member States has applied the requirements of the CBDF Package to non-EU AIFMs.

The UK has not yet implemented requirements in its domestic regime equivalent to those in the CBDF Package.

New Prudential Rules for EU Investment Firms

A new EU prudential regime for investment firms has applied from 26 June 2021. The Investment Firm Regulation (IFR) and Directive (IFD) comprise a set of legal rules which amended the existing prudential framework applicable to investment firms in the EU authorized under MiFID. The new regime provides certain changes to the risk management, regulatory capital and remuneration requirements applicable to such EU firms.

The new IFR/IFD rules apply to investment advisers, portfolio managers and corporate finance advisers, amongst others. Previously, EU firms that are authorized under MiFID were subject to varying regulatory capital requirements depending on the investment services and activities for which they are authorized and their ability to hold client money or assets. Different firms, therefore, were subject to different regimes. However, this is longer be the case as the IFR/IFD rules applies to all MiFID authorized firms, except those which are deemed to be "systemically large investment firms" (being extremely large firms typically with assets over €15 billion and which deal on their own account or carry on underwriting services). These extremely large firms remain subject to the Capital Requirements Directive IV and Capital Requirements Regulation, rather than the IFR/IFD. EU investment managers which manage assets for their clients would not typically fall within the "systemically large investment firms" designation.

The exact impact of the IFR/IFD rules on MiFID-authorized firms depends on the relevant firm's size and activities. Firms designated as "non-systemically important investment firms" were subject to changes to

capital and remuneration, governance and risk-management requirements as noted above. Smaller firms designated as "small and non-interconnected investment firms" are subject to certain capital requirements but the remuneration, governance and risk management requirements do not apply.

The new regulatory capital requirements requires all firms subject to the IFR/IFD to hold an "initial capital" requirement as well as an additional capital amount by reference to their "annual fixed overheads."

The remuneration requirements under the IFD framework applies to individuals who are senior managers, risk-takers, and staff engaged in controlled functions and certain other highly paid functions within the relevant firm. Under the rules, there is no cap imposed on "variable remuneration," but certain restrictions may apply depending on factors such as the size and complexity of the relevant firm, and firms are required to set "appropriate" fixed-to-variable remuneration ratios.

New Prudential Rules for UK Investment Firms to be effective from 1 January 2022

The UK FCA will implement its own prudential regime for investment firms (UK IFPR), based on achieving similar outcomes as IFR/IFD but tailored to apply to the UK financial services sector (particularly in light of Brexit). UK IFPR will come into effect on 1 January 2022 and further information on UK IFPR is available in the Proskauer Briefing - The UK Investment Firms Prudential Regime Effective 1 January 2022: Key considerations for Investment Firms - Insights - Proskauer Rose LLP.

New ESG Disclosure Requirements for Asset Managers in 2021

A new EU regime on sustainability-related disclosures in the financial sector came into force on 10 March 2021.

The new rules have a wide scope and will impose ESG requirements for a wide range of "financial services participants," including investment firms and fund managers which will include non-EU fund managers such as US fund managers, which market funds in the European Economic Area (EEA) under the NPPR.

The two key aspects are the EU Taxonomy Regulation (2018/0178 (COD)) and the Regulation on Disclosures (EU/2019/2088)—(referred to as the Disclosure Regulation or the SFDR).

The Taxonomy Regulation aims to establish an EU-wide classification system (or taxonomy) intended to provide firms and investors with a framework to identify the degree at which their economic activities can be considered to be environmentally sustainable. It serves to establish a common language and a classification tool to help investors and companies make informed investment decisions as to what can be considered environmentally sustainable economic activities. The provisions of the Taxonomy Regulation will start to apply from 31 December 2021 and will be phased in.

The SFDR introduces obligations on investors and asset managers to disclose how they integrate ESG factors into their risk processes.

Firms in scope will (to varying degrees) have to integrate ESG factors into their investment decision-making processes, fund documentation and website as part of their duties towards investors and beneficiaries. It is important to note that firms and advisers will be subject to additional disclosure obligations when the financial product promotes environmental and social characteristics, or has sustainable investment as part of its objective or has a reduction in carbon emissions as its objective. The majority of the SFDR provisions applied from 10 March 2021. However, there has been a delay to the finalization of the delegated legislation measure contained within the SFDR Regulatory Technical

Standards which further defines the form and content that the financial product level disclosures and reporting mush comply with. Firms in scope of the rules should monitor ongoing regulatory developments and plan accordingly.

New UK ESG Disclosure Regime

The UK proposes to implement its own measures that are broadly aligned with EU sustainability measures and has set out certain ESG guiding principles which will be at the core of its regime and has consulted on a on new climate-related disclosure requirements for asset managers with a phased-in approach starting 1 January 2022 for the largest firms with over £50 billion assets under management. From 1 January 2023, the disclosure requirements will apply to asset managers with £5 billion assets under management. The new disclosures are based on the recommendations of the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD) and will likely indirectly impact non-UK managers whereby UK asset managers will need to request certain information to meet their own disclosure obligations. Hence, firms in scope of the rules should monitor ongoing regulatory developments in the UK and plan accordingly.

UK Tax

New UK Asset Holding Company Regime

The most significant UK tax development for the funds industry this past year has been the confirmation that the new UK asset holding company (UKAHC) regime will be introduced from next April. This is an important element of the general UK fund review that the UK's tax authority (HMRC) and Treasury have been undertaking over the past couple of years aimed at making the UK a more attractive jurisdiction for setting up and administering private funds.

This initiative is a response to a number of recent developments relevant to the establishment and operation of private funds, including the introduction of the AIFMD, Luxembourg's creation of the "SCSp" as a limited partnership vehicle suitable for international private funds, Brexit and the BEPS-related international tax developments aimed at ensuring that cross-border structures have sufficient commercial purpose to be entitled to tax benefits, such as those made available under double tax treaties. All of these developments have led to an increasing number of private funds being established outside the UK and also to it becoming more important (or the perception that it is more important) that fund vehicles, their administration and their investment holding structures are all located in the same jurisdiction (the so called "co-location" principle) . In this context, the UK fund regime review and UKAHC rules are intended to enhance the UK's competitiveness as a location for asset management and to assist the UK financial sector in maintaining and increasing its market share in this area.

After a period of consultation with representative bodies, the UK Government published on 4 November the (nearly) final legislation in the draft Finance Bill 2021. These rules will be included in the Finance Act 2022 and will take effect from 1 April 2022. The regime is elective, so that a company that wishes to be treated as a UKAHC must elect to be one.

Why is the UKAHC regime required?

As stated, a number of changes over the past decade or so have resulted in a move towards European focused private funds being set up in Luxembourg rather than in the UK. The initial cause of this was the introduction of the AIFMD in 2011 and Luxembourg's creation, at the same time, of the "SCSp" as a

limited partnership vehicle that could be established on similar terms to, and with the simplicity from a tax perspective of, traditional limited partnerships under UK, US, Cayman Islands or Channel Islands law, and which was suitable as the main vehicle for international funds.

Where funds were managed or advised by UK businesses, the combination of needing to use an EU-based entity to provide easy marketing access to European investors and a Luxembourg SCSp fund vehicle providing UK VAT savings when compared to a UK limited partnership meant that (when UK asset managers wanted to set up a European "onshore" fund structure) the SCSp became more attractive than the traditional UK limited partnership. Where the fund could use an "offshore" fund structure (because, for instance, it did not need wide marketing access to European investors), a Channel Islands or Cayman Islands limited partnership provides VAT advantages over a UK limited partnership, as has always been the case. So, these developments led to an increasing number of European focused funds being set up in Luxembourg rather than the UK.

The other element of European fund structuring that traditionally has been set up in Luxembourg is the investment (or asset) holding company (or companies) (AHCs) that funds often establish below their main limited partnership vehicle to hold single or multiple fund investments. This is because Luxembourg has had a flexible tax regime that makes it relatively straightforward to ensure that the Luxembourg AHC would only be subject to tax on a small "margin" of the capital and income receipts that run through it and Luxembourg has a wide double tax treaty network. While prior to 2006 it was generally accepted that a company only had to be tax resident in a jurisdiction to be able to obtain the benefit of its double tax treaties, access to tax treaties has come under much greater scrutiny in recent years.

Now it is generally the case that a jurisdiction will require an AHC to be able to evidence sufficient commercial purpose and substance to give it the benefits of relevant double tax treaties. These commercial requirements have been highlighted recently by the introduction of the "principal purpose test" in many double tax treaties under the BEPS-related introduction of the tax treaty anti-abuse rule and the decision of the European Court of Justice in the so-called "Danish cases," which considered the requirements for a number of private equity fund-owned Luxembourg holding companies to benefit from the Denmark-Luxembourg double tax treaty.

These developments have led to the general consensus that it helps to establish sufficient commercial purpose and substance for a fund's AHCs if the fund itself and its administration and general management activities are in the same jurisdiction as the AHCs (often referred to as "co-location"). This has led to more of the structure around European investment funds moving out of the UK.

The UK fund regime review and UKAHC rules are intended to address this shift and make the UK a more attractive place for establishing private fund AHCs and, so, encourage the development of the UK's fund administration sector and bolster the UK as the preferred jurisdiction for establishing European focused private funds.

What does the UKAHC regime do?

As is well known, the principal objective in structuring a private fund is that the investors should suffer no more tax investing through the fund than they would have suffered investing in the fund's assets directly. Therefore, where the fund structuring includes an asset holding company (or companies), that company must not create material additional tax on cash flows from the fund's investments (including on sale) to the investors.

In the context of private equity, credit and non-UK real estate funds this requires, broadly, that the asset holding company be able to:

- receive gains on disposal of the fund equity investments and dividends from the investments tax free;
- make deductible payments on debt instruments issued to fund debt (and equity if relevant) assets so as to leave the company with a small "margin" based taxable profit; and
- receive gains and income from non-UK real estate without a material liability to tax.

The main reasons why the UK has not been an attractive jurisdiction for fund AHCs to date has been because:

- the UK's distribution rules (which can turn deductible interest into non-deductible distributions) make it difficult to ensure that taxable income can be passed through a UKAHC on a "back to back" debt instrument basis with only a small margin being subject to tax; and
- the UK's exemption for capital gains (the substantial shareholding exemption) is complex compared to and does not give as much certainty as Luxembourg's simple participation exemption.

The UKAHC regime is intended to remove these barriers by amending the tax rules applicable to UKAHCs to include:

- an exemption for capital gains on the disposal of "shares," except those which are property rich (deriving more than 75% of their value from UK land) with no requirement to meet minimum holding or other requirements;
- an exemption for capital gains received by the UKAHC from non-UK real estate;
- deductions for finance costs on securities such as profit-participating and convertible debt to offset variable returns on financial assets, subject to transfer pricing principles. This change should ensure that a UKAHC used by a credit fund would pay tax on an arm's-length profit margin based on its activity (and subject to details including the UKAHC's accounting treatment);
- no UK withholding tax on interest payments where the payment is made to a lender to the UKAHC;
- the ability to return capital to UK resident individual shareholders of the UKAHC on a share buyback or other capital return as capital, rather than as an income distribution (which is taxed at a higher rate); and
- an exemption from UK stamp duty and stamp duty reserve tax on share buybacks by a UKAHC, but not on the transfer of UKAHC shares.

These changes are intended to solve the absence in the UK tax legislation of a "tax neutral" corporate vehicle.

Eligibility conditions

For an AHC owned by a private fund (or otherwise) to be eligible for the UKAHC regime, the AHC must be at least 70% owned by "category A investors".

Category A investors include:

- qualifying funds — being collective investment schemes (CIS) or alternative investment funds (AIF) which are either widely marketed or are not "close" (which, broadly, means that there are not five or fewer investors in the fund that hold more than 50% of the interests in it);
- another UKAHC;
- certain specified types of investor, including sovereign immunes, pension schemes, charities and authorised persons carrying on a long term insurance business;
- public authorities; and
- certain types of non-UK companies wholly-owned by one or more category A investors which are not UKAHCs.

For private funds establishing UKAHCs it will, therefore, be important that the fund is a qualifying fund and that if there are any co-investors, they either hold less than 30% of the UKAHC, invest through what is itself a qualifying fund or fall within one of the tax exempt classes of investor. Representative bodies are encouraging a slight change to the published legislation that would aggregate parallel fund vehicles which might, if introduced, assist with this point.

The other main requirements for an AHC to be able to be treated as a UKAHC are that:

- its main activity is carrying on an investment business and activities ancillary to that business;
- its investment strategy does not involve the acquisition of listed securities; and
- none of its shares are listed or traded on a recognised stock exchange.

While on the face of it, the draft legislation is relatively detailed, so that any funds planning to establish a UKAHC will need to be confident that they will qualify and that it is not likely that they might cease to qualify in the future, it does provide the basis for what might well turn out to be an attractive regime for UK asset holding companies.

Why will a fund choose to use UKAHCs?

The problem that the UK Government faces in using the UKAHC regime to try to support the UK private fund sector generally is that it is a relatively easy and well-trodden structuring option to set up AHCs in Luxembourg.

The hope is that where private fund houses have well established asset management businesses in the UK, it will be easier to justify commercial purpose and substance for a UKAHC than for one set up in a jurisdiction in which the real value generation is not established. So, although setting up AHCs in a jurisdiction like Luxembourg has its advantages, the cost of operating in a different jurisdiction and operational complexity of having to rely on local directors and service providers to manage the AHC and the associated administration are disadvantages. It is much simpler and cheaper for a UK-based asset management business to operate its AHCs in the UK than outside the UK all other things being equal.

If UKAHCs do become popular then the co-location principle referred to above might also lead to more fund vehicles being established and administered in the UK in a virtuous circle for the UK funds sector. This will, of course, require the UK Government to make other changes to retain the UK's competitiveness in this area, including ensuring that UK-managed funds can market themselves easily in Europe.

As a very early indicator, the British Private Equity and Venture Capital Association took a straw poll of delegates at its recent Tax, Legal and Regulatory Conference and, of those responding, 55% said that they would be likely to use the UKAHC regime as soon as it is introduced, 24% said that they would wait and see how the market developed and 21% said that they thought there was still further work to be done to address all concerns. This bodes well for the use of the new UKAHC regime, albeit on a very preliminary basis.

The other current development that might help with the success of the UKAHC regime is the EU's current initiative, launched on 20 May 2021, on fighting the use of shell entities to obtain tax advantages. This initiative is to challenge the use of legal entities with no or minimal substance which perform no or very little real economic activity and are used in aggressive tax planning structures. The output might be new rules specifying new substance requirements and indicators of "real economic activity" for tax purposes which, depending on how stringent they are, might make it increasingly difficult for AHCs in jurisdictions such as Luxembourg to justify their existence and/or for funds and their investors to be confident that such AHCs will continue to have access to the tax benefits they have today.

Given the competitive nature of international rules seeking to attract private fund activity, we will have to wait (possibly not too long) to see whether the new UKAHC regime does prove popular and will stimulate the UK fund sector in the manner hoped for.

China

On February 5, 2021, the China Securities Regulatory Commission (CSRC), the regulator of the securities industry in China, issued the Guidelines on the Application of Regulatory Rules – Disclosure of Information on the Shareholders of Companies Applying for an IPO (CSRC Guidelines). The Shanghai Stock Exchange (SSE) and the Shenzhen Stock Exchange (SZSE) subsequently issued their respective detailed rules on the implementation of the CSRC Guidelines on the STAR Market and the ChiNext market (Implementation Rules).

Strengthening regulatory oversight of shareholder information disclosure by pre-IPO companies

The objective of the CSRC Guidelines is to strengthen regulatory oversight of shareholder information disclosure by companies seeking to have an IPO in China (Pre-IPO Companies). The CSRC Guidelines focuses on reviewing the following three types of shareholding arrangements of Pre-IPO Companies:

(i) Where an investor's direct or indirect ownership in a Pre-IPO Company was or is held through a nominee shareholder pursuant to a shareholding entrustment arrangement, especially in relation to PRC investors. A shareholding entrustment arrangement is required to be terminated before the concerned Pre-IPO Company files its IPO application;

(ii) Where a shareholder made a "surprise share purchase" before the Pre-IPO Company goes public. A shareholder who invested in a Pre-IPO Company within the 12-month period prior to the Pre-IPO Company's IPO application is required to lock up their shares for 36 months following the IPO; and

(iii) Where a shareholder purchased shares of a Pre-IPO Company at an abnormal purchase price, especially in relation to multi-level nested indirect shareholders.

Responsibilities and obligations of issuers and intermediaries

Under the CSRC Guidelines and its Implementation Rules, intermediaries like underwriters and lawyers are required to carry out inspection on the shareholders (direct and indirect) of Pre-IPO Companies, and

issuers/Pre-IPO Companies are required to disclose relevant shareholder information in their prospectuses and make relevant undertakings in respect of the eligibility of their shareholders.

Impacts on offshore private equity funds holding shares in Pre-IPO Companies

As a part of the above-referenced inspection conducted by intermediaries (*e.g.,* underwriters and lawyers) on the shareholders of an issuer/Pre-IPO Company, an offshore private equity fund that directly or indirectly holds shares in the issuer/Pre-IPO Company (Offshore PE Fund Shareholder) would be required by the intermediaries to:

(i) Provide its organizational documents, including without limitation its certificate of incorporation, certificate of incumbency, register of members, register of directors, memorandum and articles of association or limited partnership agreement (as applicable), and other related documents;

(ii) Complete a shareholder due diligence questionnaire, in which the Offshore PE Fund Shareholder would be required to provide relevant information in relation to its shareholding in the issuer/Pre-IPO Company, including the source of its funds, its affiliation with other shareholders, directors, officers or intermediaries of the issuer/Pre-IPO Company (if applicable), and other related information;

(iii) Provide an ownership structure chart of the Offshore PE Fund Shareholder and sign an undertaking letter confirming that there are no PRC domestic persons behind the Offshore PE Fund Shareholder;

In principle, this ownership structure chart should show the name and shareholding percentage of each direct and indirect shareholder of the Offshore PE Fund Shareholder, up to the level of ultimate beneficial owners (the UBOs) at the very top, such as individuals, listed companies, pension funds, public foundations or similar entities (not including private equity funds which are not considered as UBOs for this purpose). In practice, to a certain extent, this requirement is negotiable with the intermediaries who will determine on a case-by-case basis the level to which the identity of the indirect shareholders of an Offshore PE Fund Shareholder must be disclosed;

(iv) Sign an undertaking letter confirming that the ownership of the Offshore PE Fund Shareholder in the issuer/Pre-IPO Company is clear, does not involve a shareholding entrustment arrangement, and there has been no dispute over such ownership; and

(v) Provide certain additional documents and make relevant undertakings if the Offshore PE Fund Shareholder purchased the shares of the issuer/Pre-IPO Company within the 12-month period prior to the Pre-IPO Company's IPO application or at an abnormal price.

It is worth noting that not necessarily all the shareholder information provided to the intermediaries will be disclosed in the prospectus of the issuer/Pre-IPO Company, but the Chinese regulators could get access to such information.

Case study

In a most recent IPO case, the following shareholder information of an Offshore PE Fund Shareholder was disclosed in the prospectus of the issuer/Pre-IPO Company:

(i) The identity of the general partner of the Offshore PE Fund Shareholder and each of its direct and indirect shareholders until the individual level, and their respective shareholding percentages; and

(ii) The identity of the top 10 limited partners of the Offshore PE Fund Shareholder, their respective shareholding percentages in the Offshore PE Fund Shareholder and a general description of the types of entities they are (*e.g.*, pension fund, fund of funds, etc.).

The identity of the other limited partners of the Offshore PE Fund Shareholder was not disclosed in the prospectus. Instead, the prospectus included a general description of the types of entities such other limited partners are. The issuer/Pre-IPO Company, based on relevant undertakings made by the Offshore PE Fund Shareholder, confirmed in the prospectus that (x) there are no PRC domestic persons behind the Offshore PE Fund Shareholder, and (y) the price at which the Offshore PE Fund Shareholder purchased the shares of the issuer/Pre-IPO Company is not abnormal.

China's New Data Security Law and Personal Information Protection Law

China's data security and privacy laws have been developing rapidly in recent years. On June 10, 2021, the Standing Committee of the National People's Congress (NPC) of the People's Republic of China (China or the PRC) passed the Data Security Law of the PRC (DSL), which took effect as of September 1, 2021. On August 20, 2021, the Standing Committee of the NPC passed the Personal Information Protection Law of the PRC (PIPL), which took effect as of November 1, 2021. The DSL, the PIPL and the Cybersecurity Law of the PRC (CSL, which took effect as of June 1, 2017) form the three pillars of China's data protection regulatory framework, which govern data security, personal information protection and cybersecurity, respectively.

1. The DSL

As China's first national law governing data security, the DSL represents the Chinese government's continuing efforts to protect data security and regulate cross-border data transfers.

Scope and extra-territorial applicability. The DSL not only regulates data processing activities carried out within the territory of China, but also regulates data processing activities performed outside of China that could jeopardize the national security or public interest of China or the legitimate rights and interests of citizens or organizations in China.

Hierarchical data classification management and protection system. The DSL provides for a hierarchical data classification management and protection system that takes into account the importance of specific types of data to China's economic and social development, as well as the degree of harm that could result from a security incident. Under this system, some special data including important data and national core data are protected by stricter regulatory measures.

- National Core Data. National core data is a new category of data introduced in the DSL. The DSL defines national core data as data related to national security, the lifeline of the national economy, important aspects of people's livelihoods and major public interests. Under the DSL, national core data is subject to stricter regulations and more enhanced processing restrictions than important data or general data.

- Important data. The concept of important data was first introduced in the CSL, in which network operators in China are required to categorize data and create backups and encryption measures for the protection of important data. For important data under the DSL, business operators must appoint a responsible person, establish a specific internal department for the protection of important data, carry out risk assessments on a regular basis, and report the results to the relevant Chinese regulators.

Data localization requirement and restrictions on cross-border data transfer. The DSL introduces separate frameworks for the regulation of cross-border transfers of important data by critical information infrastructure (CII) operators and non-CII operators. For CII operators, cross-border transfers of important data collected and generated by them in China is governed by the CSL and is subject to a

security assessment by the relevant Chinese regulators. For non-CII operators, the DSL provides that the Cyberspace Administration Office (CAC), China's top cyberspace regulator, will formulate and issue separate rules applicable to cross-border transfers of important data collected and generated by non-CII operators in China. The DSL expressly prohibits provision of any data stored in China to judicial or law enforcement agencies outside of China without prior approval from the relevant Chinese governmental authorities.

Government access to data and export control. Under the PIPL, individuals and entities are required to cooperate with the public security and state security authorities that need to access data for the purpose of safeguarding national security or investigating crimes. This provides a legal basis for the Chinese government to access data of businesses. The PIPL includes provisions that expands China's export control regime to cover the export of data and provides a legal basis for the Chinese government to impose reciprocal measures on any country or region that imposes discriminatory prohibitions, restrictions or other similar measures against China in terms of investment and trade related to data and data development and use technologies.

Legal liabilities for violations. The DSL imposes severe punishments for entities violating the law, including suspension of business, revocation of business license, fines up to RMB 10 million (approximately US$1,560,000), and potential criminal penalties. Individuals directly responsible for a violation may be subject to a personal fine up to RMB 1 million (approximately US$156,000) and potential criminal penalties. Entities may be punished for a failure to cooperate with the Chinese regulators' data requests, and for providing data to foreign judicial or law enforcement agencies without approval from the relevant Chinese governmental authorities.

2. The PIPL

As China's first comprehensive legislation on personal information protection, the PIPL sets forth detailed rules with respect to data privacy and personal information protection in China.

Scope and extra-territorial applicability of the PIPL. The PIPL not only regulates data processing activities carried out within the territory of China, but also regulates data processing activities performed outside of China involving personal information of individuals located in China where the processing is (a) for the purpose of providing products or services to individuals located in China, (b) for the purpose of analyzing and evaluating the behaviors of individuals located in China, or (c) for other purposes provided by laws and regulations. Under the PIPL, offshore companies engaging in the processing of personal information of individuals located in China are required to designate an agency or a representative in China to be responsible for matters related to personal information protection. The name and contact details of such local agency or representative are required to be provided to the relevant Chinese regulators.

Personal information and sensitive personal information. The PIPL defines personal information as any type of information that is recorded electronically or by other means and identifies or can be used to identify a specific individual, excluding anonymized information. The PIPL defines sensitive personal information as the personal information the leakage or illegal use of which may lead to harm to the dignity of individuals or serious harm to personal safety or property, including information relating to biometric characteristics, religious beliefs, specially designated status, medical health, financial accounts, individual location tracking, and the personal information of minors under the age of 14, and set outs more stringent obligations on processors handling sensitive personal information.

Legal grounds for processing personal information. Under the PIPL, processing of personal information is not permitted unless a legal ground for such processing exists. In addition to the "notification and consent" legal ground for processing personal information provided in existing personal information protection rules and regulations, the PIPL also includes the following legal grounds for processing personal information:

- necessity for concluding or performing contracts to which the individual concerned is a party;

- necessity for employees and human resources management in accordance with legally adopted internal regulations and legally concluded collective contracts;
- necessity for performing legal duties or legal obligations;
- to respond to public health emergencies, or necessity for the protection of the life, health, and property of individuals in an emergency;
- processing, within a reasonable scope, of personal information for news reporting and supervision of public opinion for the public interest; and
- processing, within a reasonable scope and in accordance with the PIPL, of personal information that has been made public by the concerned individual or through other lawful means.

Data localization requirement and restrictions on cross-border data transfer. Under the PIPL, CII operators and entities that process personal information that reaches a certain threshold (to be specified in subsequent implementation rules) must (i) store locally in China the personal information they collect and generate in China and (ii) pass a security assessment administered by the CAC and other enforcement authorities to the extent they seek to transfer personal information outside of China.

Other personal information processors may conduct cross-border transfer of personal information upon satisfying one of the following requirements: (a) passing a security assessment by the CAC; (b) obtaining certification of data security by a professional body recognized by the CAC; (c) entering into an agreement with the overseas recipient with provisions governing the rights and obligations of the parties based on a template contract to be released by the CAC; or (d) other requirements as provided by relevant laws and regulations.

Legal liabilities for violations. Depending on the severity of the violation, the PIPL confers the relevant Chinese regulators with different powers to address any violation of the PIPL, including issuing a correction order or warning, confiscating unlawful gains, ordering the suspension or cessation of a business, revocation of business license and/or imposing fines up to RMB 50 million (approximately US$7.8 million) or 5 per cent of the personal information processor's turnover in the previous year. In addition, individuals directly responsible for a violation may be subject to a personal fine ranging from RMB 100,000 (approximately US$15,600) to RMB 1 million (approximately US$156,000), and may also be prohibited from holding certain management and director positions for a certain period of time.

Hong Kong

Introduction of Carried Interest Tax Exemption

In our 2020 Report, we reported that in August, 2020, the Hong Kong Government had issued a consultation paper containing a proposal to provide a tax concession for carried interest for private equity funds at a competitive rate. This followed considerable lobbying efforts by the local fund management industry for a relaxation of local tax treatment of carried interest.

The new tax concession on carried interest earned from the activities of private equity funds was introduced in May, 2021, by way of amendment to the Inland Revenue Ordinance (IRO). Under this new concession, eligible carried interest received or accrued on or after from 1 April, 2020 will be subject to zero percent profits tax. And individuals who have received carried interest or to whom any such sum has

accrued, will also be eligible for a 100% deduction for those sums against their assessable income. For further details of this tax concession, see our Client Alert on this topic.

A particular feature of the tax concession regime is that the fund from which the carried interest is ultimately earned, must be certified by the Hong Kong Monetary Authority. The purpose of the certification requirement is to verify that the fund is in compliance with certain baseline criteria set out in the IRO to qualify for the tax concession. The Inland Revenue Department will then assess whether the fund as certified by the HKMA together with other conditions required by the IRO, qualifies for the tax concession. The HKMA published its guidelines for certification[6] in July this year.

SFC Licenses First Virtual Asset Trading Platform

The SFC announced in mid-December 2020 that it had granted the first licence to a virtual asset trading platform in Hong Kong under the licence types, Type 1 (dealing in securities) and Type 7 (providing automated trading services) regulated activities (RAs). As part of its licensing condition, the platform is only able to serve "professional investors"[7] under the close supervision of the SFC and is subject to tailor-made requirements similar to those which apply to securities brokers and automated trading venues.[8]

In November 2019, the SFC introduced a comprehensive framework for the regulation of virtual asset trading platforms[9] which is consistent with the recommendations of international standard-setting bodies.[10]

Additionally, in May 2021, the Hong Kong Government published its conclusions to its consultation paper on a new legislative framework which would make the SFC the regulator of all centralised virtual asset (VA) exchanges, including those that only trade types of virtual assets which currently fall outside the SFC's jurisdiction.

It is proposed to designate the business of operating a VA exchange as a "regulated VA activity" under the Anti-Money Laundering Ordinance and Counter-Terrorist Financing Ordinance (AMLO) and require that any person seeking to operate a VA exchange in Hong Kong apply for a licence from the SFC as a licensed VA service provider under the AMLO. A VA exchange is to be defined as any trading platform which is operated for the purpose of allowing an offer or invitation to be made to buy or sell any VA in exchange for any money or any VA, and which comes into custody, control, power or possession of, or over, any money or any VA at any point in time during its course of business. Peer-to-peer trading platforms (*i.e.*, a platform does not provide any trade matching mechanisms), to the extent that the actual transaction is conducted outside the platform and the platform is not involved in the underlying transaction by coming into possession of any money or any VA at any point in time, would not be covered by the VA exchange definition.

The Government has indicated that it targets to put forward the draft legislation to regulate VA exchanges in the 2021-22 legislative session.

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[6] See Hong Kong Monetary Authority - Competitive International Financial Platform (hkma.gov.hk).

[7] As defined under the Securities and Futures Ordinance and related rules.

[8] See the SFC's Terms and Conditions for Virtual Asset Trading Platform Operators

[9] In its Position paper, Regulation of virtual asset trading platforms, of 6 November 2019, the SFC announced a regulatory framework for virtual asset-trading platforms which offer trading of at least one security token.

[10] See the IOSCO Final Report, "Issues, Risks and Regulatory Considerations Relating to Crypto-Asset Trading Platforms" published in February 2020.

Additional Guidance to Market Participants on External Electronic Data Storage

In December, 2020, the SFC issued additional guidance to market participants on external electronic data storage in response to questions from LCs and other stakeholders.[11] The guidance is in the form of frequently asked questions in relation to the SFC's circular of 31 October 2019 that sets out requirements for using external electronic data storage providers (EDSP) to exclusively keep records or documents required under the Securities and Futures Ordinance (SFO) or the AMLO. The SFO requires that an LC shall not use any premises for the keeping of records or documents relating to the carrying on of the RA for which it is licensed without the SFC's prior written approval. A particular requirement contained in the 2019 circular is to ensure that the LC and the SFC can secure access to all the LC's "Regulatory Records"[12] within the territory whenever required.

The 2019 circular required that where any Regulatory Records of an LC are kept exclusively with an EDSP, the LC will be required to provide the SFC with a notice from it to the EDSP authorising and requesting it to provide the LC's records to the SFC, and counter-signed by the EDSP as evidence of its recognition of such authorisation and request. And if the EDSP is not Hong Kong based, the LC will also be required to have the EDSP sign an undertaking to the SFC which will include an obligation to disclose and transfer to the SFC both the LC's data and the EDSP's audit trail of access for that data (*e.g.,* audit logs showing access to the data, including generation and modification of the data), and to provide all necessary assistance to the SFC in the performance of its functions and powers.

Under the 2020 guidance, as an alternative means of satisfying the requirements in the circular, the SFC will accept an undertaking from each of the LC's two Managers-In-Charge of Core Functions or, with the SFC's consent, one Manager-In-Charge or one Responsible Officer. The alternative is available only if certain conditions are satisfied by the LC such as: the LC maintains a document which provides an overview of how electronic Regulatory Records are stored exclusively with affiliates and/or EDSPs (*i.e.*, an Access Map) which broadly identifies the types of electronic Regulatory Records which are stored exclusively with each affiliate or EDSP, and the physical locations of the data centres or other premises where the electronic Regulatory Records are stored; and the LC ensures its operational resilience and performs a daily backup of electronic Regulatory Records to ensure that a set of complete and up-to-date records are maintained which are sufficient to account for the following: (a) client transactions; (b) outstanding client positions; and (c) client assets held by the LC or its associated entity.

Upgrading of Industry Practitioners' Competency Standards

The SFC has published revised Guidelines on Competence, Guidelines on Continuous Professional Training and Fit and Proper Guidelines which will become effective on 1 January 2022. The revisions represent the first major update to the Guidelines on Competence since 2003.

An individual applying to the SFC for a licence as a Responsible Officer or a Licensed Representative of a licensed corporation (LC) which will carry on an RA must satisfy the SFC's entry *competence* requirements to demonstrate that he/she is equipped with the necessary technical skills and professional expertise to be "fit", and is aware of the relevant ethical standards and regulatory knowledge to be "proper" in carrying on RAs. These requirements have historically required the applicant to satisfy the SFC as to the following for Responsible Officers: (i) academic, professional or industry qualifications,

[11] See the Hong Kong section of our 2020 Report under "SFC issues guidance for LCs on external electronic data Storage".

[12] The phrase "Regulatory Records" is not defined in legislation but refers to any records and documents required to be kept by the LC under the SFO or the AMLO

(ii) relevant industry experience, (iii) management experience, and (iv) local regulatory knowledge. The equivalent requirements for Licensed Representatives are less stringent.

The revisions include:

(i) The raising of the minimum academic qualification requirements for individuals whilst at the same time broadening the scope of recognised academic qualifications. Current licensees will be grandfathered under the revised Guidelines to minimise any potential impact to existing practitioners and institutions.

(ii) Introducing a full exemption from obtaining recognised industry qualifications for temporary licence applicants.

(iii) Recognising a broader range of experience as being relevant when considering individual applications seeking accreditation to private equity managers.

(iv) Accepting as management experience, experience acquired in the "financial industry" on the basis that such experience is more transferrable across RAs.

Expansion of Shanghai-Hong Kong Stock Connect

Effective 1 February, 2021, new arrangements went into place that expanded the Shanghai-Hong Kong Stock Connect programme between The Stock Exchange of Hong Kong Limited (SEHK), and the SSE and the SZSE. The programme was originally introduced in 2014, was further expanded with the launch of Shenzhen Connect in 2016, and the launch of Bond Connect in 2017. The new arrangements are these:

Northbound Trading

The Northbound trading now includes A+H companies listed on the STAR Market that are constituent stocks of the SSE 180 Index and SSE 380 Index, or have H-share counterparts listed in Hong Kong, under the existing Stock Connect arrangements.

Likewise, their corresponding H-shares listed on the SEHK are now included in Southbound trading under the existing Stock Connect arrangements.

Given that there are special investor eligibility requirements for the STAR Market, STAR Market-listed shares will only be accessible via Northbound trading of Stock Connect by "institutional professional investors" as defined under the SFO.

Southbound Trading

The Southbound trading arrangements now include shares of pre-revenue biotech companies listed on the SEHK that are eligible constituent stocks of the Hang Seng Composite Index, or have corresponding A-shares listed on SSE or SZSE.

Likewise, shares of biotech companies that are H-shares in STAR Market-listed A+H companies are also now included in Southbound trading of Stock Connect under the inclusion arrangements for STAR Market-listed shares referred to above.

Climate-related Risks for Fund Managers

In August 2021, the SFC issued amendments to the Fund Manager Code of Conduct (FMCC)[13] and a circular setting out expected standards for fund managers managing collective investment schemes to take climate-related risks into consideration in their investment and risk management processes and make appropriate disclosures. The new requirements which cover four key elements, namely governance, investment management, risk management and disclosure, will be implemented in phases with the first phase to begin on 20 August 2022 (see below).

In proposing these amendments, the SFC made reference to the Task Force on Climate-related Financial Disclosures Recommendations in developing the requirements and also considered the global regulatory trend towards harmonisation and comparability of standards across jurisdictions.

This circular sets out the expected standards for complying with the amended FMCC, including (i) baseline requirements for all those managing collective investment schemes (CIS) and (ii) enhanced standards for fund managers with CIS under management which equal or exceed HK$8 billion[14] in fund assets for any three months in the previous reporting year (Large Fund Managers).

The SFC's requirements are applicable based on the relevance and materiality of climate-related risks to the investment strategies and funds managed by the fund managers as well as their roles. Fund managers will be required to apply the principle of proportionality[15] in determining how to comply with the requirements. Where fund managers delegate the investment management function to sub-managers, they retain the overall responsibility for complying with the SFC's requirements.

The new regulatory requirements will become effective after the following transition periods:

- a 12-month transition period for Large Fund Managers to comply with the baseline requirements (*i.e.*, until 20 August 2022) and a 15-month transition period for them to comply with the enhanced standards (*i.e.*, until 20 November 2022); and
- a 15-month transition period for other fund managers to comply with the baseline requirements (*i.e.*, until 20 November 2022).

Revised SFC AML/CFT Guidelines

Following the publication of its consultation conclusions on proposed amendments to its Anti-money Laundering and Counter-financing of Terrorism (AML/CFT) Guidelines (for licensed corporations), revised SFC AML/CFT Guidelines came into effect on 30 September 2021, with the exception of the new cross-border correspondent relationships requirements, which will take effect on 30 March 2022.

The revisions were made to align the SFC Guidelines with the Guidance for a Risk-based Approach for the Securities Sector (RBA Guidance for the Securities Sector) published by the Financial Action Task Force (FATF) in 2018, to address some areas for improvement identified in the latest FATF Mutual

[13] The FMCC sets out conduct requirements for persons licensed by or registered with SFC whose business involves the management of collective investment schemes (whether authorised or unauthorised) and/or discretionary accounts (in the form of an investment mandate or pre-defined model portfolio).

[14] This threshold does not include assets under discretionary account management.

[15] Assessing the nature, size, complexity and risk profiles of the fund managers and the investment strategies adopted by each fund under their management.

Evaluation Report of Hong Kong published in September 2019 relevant to LCs, and to provide practical guidance to facilitate the implementation of AML/CFT measures in a risk-sensitive manner.

The RBA Guidance for the Securities Sector was developed by the FATF taking into account the experience of the private sector over the years. It outlines the key principles for applying a risk-based approach in the securities sector and provides practical guidance to securities sector participants on adopting risk-based procedures to prevent ML/TF.

The main revisions to the SFC Guidelines address these aspects of the RBA Guidance for the securities sector:

- the process and methodology of ML/TF risk assessment as well as indicators of a higher or lower risk level associated with specific risk factors which should be considered in the assessment; and
- the risk mitigating policies, procedures and controls for CDD and ongoing monitoring in various risk situations measures, including:
- additional measures to mitigate the risks associated with business relationships in the securities sector similar to cross-border correspondent banking relationships;
- simplified and enhanced measures for customers assessed to be either of lower or higher ML/TF risk; and
- red-flag indicators of suspicious transactions and activities.

Introduction of Investor Identification and OTC Securities Transaction Reporting

An investor identification regime is expected to be launched in the second half of 2022 and the OTC securities transactions reporting regime in the first half of 2023, subject to the completion of system testing and market rehearsals. The regime is intended to facilitate more timely and effective market surveillance, and reduce ongoing compliance costs in dealing with SFC enquiries about client identities. It would be in line with developments in major jurisdictions, including those in the United States, Europe, Australia, Singapore and Mainland China.

Currently, only the information for an Exchange Participant which inputs a securities order (but not that of its underlying client which instructed the order) is captured by the trading system used by the SEHK.

Under the new reporting regime, LCs and registered institutions would submit to the SEHK the names and identity document information of clients placing securities orders on SEHK at the trading level, as well as for off-exchange orders which are reportable to SEHK.

Information on OTC securities transactions in ordinary shares and real estate investment trusts listed on SEHK will be reported to the SFC under a separate regime.

The LC or registered institution submitting the order or reporting the trade would also be required to include a unique identification code assigned to the relevant client.

To implement the regimes, revisions will be made to the Code of Conduct for Persons Licensed by or Registered with the SFC, to become effective on a date to be determined by the implementation timelines.

Latin America

Recent Trends in Private Equity and Venture Capital

Despite the challenges posed by the continuing pandemic, the GPCA (Global Private Capital Association) Mid-Year 2021 analysis found that private capital investment in Latin America continues to increase on a year-on-year basis as measured for the first half of 2021 (139% for H1-2021 vs. H1-2020) driven by investments in tech-focused enterprises and logistics. Private equity investors, large pensions and sovereign wealth funds are also increasing their investment focus in the region after backing Asian startups in the previous years.

In Brazil, the private equity and venture capital market has proven its endurance: not only has the total capital raised during 2020 surpassed the pre-pandemic volume two fold (BRL6.6 billion for 2019 vs. BRL12.7 billion for 2020), nearing an all-time high, but also investments during the first two quarters of 2021 have already exceeded the total invested amounts for the entire year 2020 (BRL23.6 billion for 2020 vs. BRL24.7 for Q1 and Q2 2021).

The continued growth of the private and venture capital industry seems to indicate that managers have been resilient and progressed their efforts in both fundraising and deployment of capital despite the pandemic-induced poor economic growth and inflationary pressures.

However, this growth does not come without changes. In a 2020 survey conducted by the Brazilian Private Equity and Venture Capital Association (ABVCAP) with 41 local managers, managers generally ranked segment consolidation and an acceleration of the digital economy as the two main consequences and opportunities generated by the pandemic. Private equity managers also ranked IT, agribusiness and healthcare as the first, second and third (respectively) segments most likely to benefit from the changes brought by the pandemic.

The data for investments for the two first quarters of 2021 confirms such trends, the segments most invested by private equity funds during such period were: financial services (especially digital banks) (30.3%), IT (15.2%) and healthcare (13.1%).

On the exit side, Brazil has also seen a boom in the number of IPOs in 2020 (the 28 IPOs in the year alone is close to the overall number of IPOs that took place from 2013 to 2019), a trend that has continued during the first half of 2021. This represents great news for GPs, as IPOs seem to have become another possible exit strategy in Brazil in addition to the established buyout route, as data shows that, at the time of their IPO, six out of every ten companies have private equity funds as shareholders.

Rise of Co-Investments and Secondaries

Similar to international trends in recent years, Brazil has seen a surge of co-investment opportunities in general, which may be a result of recent currency devaluation – the Brazilian Real (BRL) was one of the most devaluated currencies during the pandemic period, resulting in increased attractiveness to international investors –, the maturing of the Brazilian market, bringing it closer to international practice, increased M&A activity and segment consolidation during the pandemic, among other factors.

Unlike the international trend of fees applicable to co-investments, Brazilian co-investments still typically are structured as nil or lower fee opportunities, as GPs continue to seek to allocate these deals to investors both locally and internationally.

Secondary transactions are also a rising trend in Brazil. The first Brazilian private equity fund was established in 1996, but only in 2007 did the number of fundraisings surpass 10, with the majority taking place during the last decade. Additionally, recent research found that approximately 85% of the funds have a term equal to or longer than eight years (with the majority over 10 years). Both of these factors make for an industry where the early vintages of the majority of sponsors are now getting to the end of their life cycle.

However, similar to international data that 82% of the funds from vintage years 2005-2009 are still active, many Brazilian funds are also seeking to continue past their initially envisioned termination dates. This has led to an increase in GP-led secondaries, both in the form of continuation funds or to related parties (see *Increase in Alternatives Products* below), as well as LP-led secondaries.

With respect to the latter, Brazil has seen greater numbers of international fund-of-funds GPs entering the market and also local GPs establishing new fund-of-funds products. This trend accelerated with the increased interest of investors in Brazil for alternative products that sought a more diversified strategy (and potentially with a lower minimum investment requirement) than traditional private equity funds. These fund-of-funds have also played a larger role in secondaries in the Brazilian market, providing investors with liquidity in LP-led secondaries.

Increase in Alternatives Products

The past few months have been very transformative for the funds industry in Brazil. In addition to new regulatory rules being proposed to replace the entire existing ruleset for funds (see *Recent Legal and Regulatory Developments in Brazil* below), the Brazilian market saw the number of public offerings of private equity funds jump from 3 in 2019 (totaling BRL1.15 billion) to 15 in 2020 (totaling over BRL 9 billion).

This large increase is mostly due to the resurgence of incentivized private equity infrastructure funds (*fundos de investimento em participações em infraestrutura*, or "FIP-IE"), now being offered through public offerings to qualified investors. These funds were created under Federal Law No. 11,478, dated May 29, 2007, which exempts individuals that invest in such funds from Brazilian withholding income tax, provided that the FIP-IE complies with certain requirements, including:

- The FIP-IE shall invest in infrastructure projects initiated after January 22, 2007, in energy, transportation, water treatment and sanitation, irrigation and other key infrastructure segments selected by the Brazilian federal government;
- The FIP-IE shall have more than 5 investors and no investor may own or otherwise be entitled to economic interests of the fund in excess of 40%;
- The FIP-IE quotas must be listed on a stock-exchange; and
- The FIP-IE shall invest 90% of its net equity in securities within 180 days from its registration with the Brazilian Securities Commission.

The low interest rates registered during 2020 and increased search by Brazilian investors to diversify their investment allocation culminated in the rise of publicly-traded FIP-IE, creating a mix of private equity fund and listed investment vehicle (akin to Brazilian real estate funds) – many of which have been invested by thousands of qualified investors.

These funds also serve an attractive exit mechanism for infrastructure GPs looking to divest from developed infrastructure projects – many GPs formed FIP-IEs with longer terms (some greater than 50

years) and entered into secondary transactions with sponsored funds that developed such infrastructure projects and were reaching the end of their investment cycle.

Creation of the Brazilian Agribusiness Fund Type – FIAgros

The Brazilian agribusiness is one of the three largest segments in the Brazilian economy, representing 26.1% of Brazil's 2020 GDP according to a research report by CEPEA (Agriculture and Livestock Brazilian Confederation). Contrary to the general trend in the Brazilian economy resulting from the pandemic, the agriculture industry grew 2% from 2019 to 2020 based on data from IBGE (Brazilian Institute of Geography and Statistics), with increases of 4% in export revenues and 10% of volume for this same period.

Despite the sheer growth and importance of the Brazilian agribusiness, 2020 data from Climate Policy Initiative shows that the funding for this industry is still bank-centric, focused primarily on the largest producers and is represented by fragmented rules and credit distribution channels, as well as subject to disparate conditions for funding.

Looking to incentivize funding to the agribusiness industry, on March 29, 2021, the Brazilian Congress approved Federal Law No. 14.130, which amended certain federal laws and created a new type of investment fund in Brazil, the Brazilian Agribusiness Fund (*fundo de investimento nas cadeias produtivas agroindustriais*, or "FIAgro"). FIAgro's purpose is to foster investments in the Brazilian agribusiness through the capital markets by exempting individuals that invest in such funds via stock exchange from Brazilian withholding income tax, provided that the fund has at least 50 investors with none of them holding (or otherwise being entitled to economic benefits representative of) more than 10% of the interests of the fund.

Pursuant to the law, FIAgros may invest their portfolios in:

- Farmlands and other rural real estate;
- Equity interests in entities that participate in the agro-industrial productive chain;
- Financial assets, title instruments and other securities issued by individuals and entities that participate in the agro-industrial productive chain;
- Receivables and other collateralized titles backed by receivables related to agribusiness;
- Real estate receivables linked to rural real estate and other securities backed by such receivables; and
- Quotas of other Brazilian investment funds (fund of funds) that invest more than 50% of their net equity in such assets.

The FIAgro law also granted ample powers to the Brazilian Securities Commission (*Comissão de Valores Mobiliários*, or CVM) to regulate FIAgros. On July 13, 2021, the CVM issued a temporary ruling (CVM Resolution No. 39) establishing FIAgros as sub-categories of existing fund types, namely: receivable funds (FIDC) FIAgro, real estate (FII) FIAgro and private equity (FIP) FIAgro.

This decision was likely made due to the fact that the CVM has announced it expects to refresh the entire fund regulation in Brazil in the near future (see *Proposed New Regulatory Framework for Investment Funds* below), providing for a complete and more extensive (and potentially separate) regulation for FIAgros under that cover. Nevertheless, we understand CVM Resolution no. 39 was issued with the intent to test the market for this type of fund, which can now be created as tax-incentivized vehicles formed in accordance with the rules applicable to either of the three types of investment funds listed above.

Growth of Venture Capital

On the venture capital side, Brazil has seen sustained increase in venture capital investments during the past years, reaching an all-time high in 2020. During the first half of 2021, the total investments by venture capital funds surpassed investments of private equity funds both in number of deals and in total invested volume (which has already exceeded the 2020 year amounts).

This growth is likely a result of the combination of a more mature market with increased number of VC-backed unicorns and the digital push accelerated by the demands of the ongoing global pandemic. International and local venture capital firms continue to fundraise and deploy available capital, while the market has seen new entrants that invested directly into rounds of portfolio companies – such as Berkshire Hathaway's investment in Nubank, Softbank's, Kaszek's and others in Gympass and Lightrock investment in Buser.

Another recent trend is the creation of international holding structures (commonly referred to as "flip") for Brazilian VC-backed companies, that serve as aggregators for future rounds of investments under investor-friendly jurisdictions, as well as a future platform for the IPO of such companies in international stock exchanges. Recent examples include PagSeguro, Netshoes, Afya, XP Investments and Vitru, among others.

Recent Legal and Regulatory Developments in Brazil

On the legislature side, the Brazilian Congress is currently debating two tax reform projects which are relevant for the funds industry: one focused in reforming the existing income tax rules applicable to individuals, entities and funds, and another focused on the creation of a value added tax to replace two existing taxes (PIS/Pasep and Cofins). While the latter seems to be stalling and has been heavily debated, the former appears to be gaining traction within the legislative members.

While still subject to changes, the current draft of the income tax reform (Federal Law Project No. 2,337/2021) includes relevant changes to the taxation of investment funds and entities, including:

- The application of phantom income tax to closed-ended funds owned by a single investor;
- Taxation of dividends (which are currently exempt) at a flat rate of 15%;
- Reduction of overall income tax rates for companies; and
- Clarifications regarding the requirements for non-resident investors to be exempt from WHT when investing in Brazilian private equity investment funds (*fundos de investimento em participações*, or FIPs).

With respect to the clarification on the WHT exemption to non-resident investors, the draft revokes paragraphs one and two of article three of Federal Law No. 11,312, which currently set out the requirements for the application of said benefit (including, among others, the 40% Test detailed in *Ongoing Developments on the Tax Scrutiny over FIP Ownership Structures* below). Instead, the draft adds a new paragraph only requiring that such non-resident investors are domiciled outside of favorable tax jurisdictions.

On the regulatory side, the CVM has published proposed rules that would represent major innovations to funds' and public offerings' regulatory framework, as described in each of the topics below.

Proposed New Regulatory Framework for Investment Funds

The first major proposed rule by the CVM in 2021 is intended to replace the current rules regulating the existing fund types in Brazil (currently dispersed in multiple segregated rules), consolidating these in a single rule, and consisted of a general section applicable to all funds and annexes that provided for specific rules applicable to each type of fund – the draft included forms of rules for receivables funds (FIDC) and financial investment funds (a new category that would encompass the current shares investment funds (FIA), fixed income funds (FIRF), currency funds (FIC) and multimarket funds (FIM)).

This proposed rule was prepared in response to the enactment of the Brazilian Economic Liberty Act (Law No. 13,874), which introduced a new statutory landmark for investment funds, among other important improvements to the corporate Brazilian legal system and other business-friendly legal topics.

Among the many innovations proposed by such rule, we want to highlight:

- Limited liability to all fund investors as a general rule (including for existing funds at the time of enactment), unless investors explicitly opt-out of such regime;
- Flexibility to create segregated portfolios with several liability for all fund types, including creation classes of interests subject to different political and economic rights within the same segregated portfolio (restricted to certain accredited investors);
- More clear cut distinction between the roles of portfolio managers and fiduciary administrators, each subject to several liability before the fund (and limited to circumstances arising from their willful misconduct and bad faith);
- Limitation of capital risk and leveraged transactions for retail and qualified retail funds; and
- Changes to the rules applicable to FIDCs, providing for greater investment flexibility for funds targeted at accredited investors, while also permitting the distribution of such funds to retail investors subject to certain restrictions.

The public consultation phased of this proposed rule was highly debated between market participants and regulators during its comment period, resulting in over ninety comment forms being submitted by managers, industry associations, law firms and others. The CVM is expected to process the comments received and publish this rule in the near future, commencing a new cycle of regulatory framework in view of the innovations brought by such rule, as detailed above.

Proposed New Regulatory Framework for Offerings of Securities

The second major rule proposed by the CVM relates to the offering of securities, including quotas of investment funds, in Brazil. Currently, offerings of securities follow two main regimes in Brazil: offerings under restricted placement efforts pursuant to CVM Instruction No. 476 (which are exempted from registration with the CVM) and full-fledged public offerings pursuant to CVM Instruction No. 400 (which are subject to prior analysis and registration with the CVM).

This new proposed rule would replace both existing rules and create a distinction based on the investor classification as either a “professional investor,” “qualified investor” or “retail investor” pursuant to CVM Resolution No. 30. All non-Brazilian investors are deemed to be professional investors.

Among the proposed changes, the distribution of interests (quotas) of Brazilian closed-ended funds to professional investors would be subject to automatic registration with the CVM and the limitation on number of investors currently applicable to restricted placement efforts (which limits offering efforts to 75 investors and investment by up to 50 investors) would no longer apply, creating a more efficient pathway to distribute funds to a larger number of accredited investors.

Similarly to the investment funds proposed rule, the CVM is still analyzing the comments sent by market participants during the public consultation phase and is expected to publish this rule in the near future.

Ongoing Developments on the Tax Scrutiny over FIP Ownership Structures

Dividends and capital gains distributed by FIPs to international investors upon the amortization or redemption of the FIPs' quotas are subject to zero percent Brazilian income tax rate (Beneficial Tax Rate) pursuant to Federal Law No. 11,312, provided that, among other requirements, no investor owns or is otherwise entitled to economic interests of the fund in excess of 40% (directly or indirectly) (the so-called "40% Test").

Brazilian administrators have been subject to tax auditing and tax assessments by the Brazilian Revenue Service which previously focused on the disclosure of the ultimate beneficial owners (UBOs) of such funds' structures.

Since then, the Brazilian Revenue Service has continued to perform new tax inspections and issue tax assessments, which seem to have shifted to a new focus —the adoption of parallel fund structures managed by the same GP and funds organized in favorable tax jurisdictions ("FTJ") such as the Cayman Islands. With respect to the former, the Brazilian Revenue Service has challenged the compliance with the 40% Test on the basis of that all such vehicles have a common manager and, under their view, a common controlling entity. With respect to the latter, the Brazilian Revenue Service has claimed that, as such funds are organized in FTJs (despite the existence of AIVs and other intermediary entities organized in non-FTJ jurisdictions such as Delaware), these do not comply with the requirement in Federal Law No. 11,312 that international investors shall not be domiciled or reside in FTJ.

Many market players, Brazilian and international law firms (including Proskauer) and certain Brazilian associations (such as ABVCAP) continue to engage in discussions with the Ministry of Economy and the Brazilian Revenue Service to develop proposed actions and changes to the existing rules to adapt these to prevailing international structures and best practices. The proposed language under the income tax reform legislation is a product of such discussions and, while we cannot anticipate if such law will be approved in its current form, we continue to follow this matter closely and engage in discussions with stakeholders and regulators.

State Regulation / Blue-Sky

Compliance with Rule 506 is very important in connection with state securities or "blue sky" laws, since, under Section 18 of the Securities Act, the states are pre-empted from regulating offerings that comply with Rule 506. Without such compliance with Rule 506, there is no pre-emption and, unless an applicable self-executing state exemption is available, a state where an investor purchases the issuer's securities can require a pre-sale filing and regulate the required disclosure for the offering as well as other aspects of the offering. If a filing is incomplete or late or a state finds any other issue with it, they may require that the issuer make a rescission offer to the investors and possibly pay fines.

Provided that an offering is made in compliance with Rule 506, the blue sky laws of many states currently require that a hard copy of Form D be filed with the relevant state authority within 15 days following the initial sale of securities in that state, along with the state's required filing fee. In addition, some states' blue sky laws require that copies of amended SEC filings also be filed with the state. A handful of states require annual renewal filings and, in a couple of cases, the payment of annual renewal fees for ongoing offerings. Please note that the states now have a central electronic filing system for Rule 506 offerings, "The NASAA Electronic Filing Depository" usually referred to as the "EFD," which is currently required to

be used for filings in 17 states, and possibly will be mandatory for all or most states in the not-too-distant future. EFD filings have become much more prevalent since the start of the pandemic.

Private funds should be aware of requirements that may be triggered when sales of securities are made to investors in states where sales have not been made in the past, and sales in states in which a Form D has not yet been filed. The penalties for failing to make timely filings can be significant. Some states may require payment of a fine, or even demand that an issuer offer rescission to each investor in a state, or the administrator may issue a consent order.

Although Section 18 of the Securities Act states that covered securities, such as securities offered pursuant to Rule 506 of Regulation D, are not subject to state regulation, an increasing number of states use their authority under broker-dealer and investment adviser regulation and anti-fraud statutes to review and comment on Form Ds filed in connection with Rule 506 offerings. Questions regarding whether a related party listed under item 3 of the Form D is required to be registered as an investment adviser in the state are not unusual. A handful of states also occasionally request to see copies of the offering materials provided in connection with the offering.

Annual and Other Periodic Filing Requirements

Below is a summary of certain key filing requirements applicable to advisers to private funds. We note that this list of filings discussed below is not intended to be exhaustive. In addition to the requirements discussed in this Annual Review, advisers should examine the nature of their business and operations and determine whether any other filings or actions will be required pursuant to applicable federal, state and non U.S. laws and regulations.

Form ADV

Registered investment advisers must file an updated Form ADV Part 1 and Part 2A with the SEC within 90 days after the investment adviser's fiscal year-end (by March 31, 2022 for advisers with a December 31 fiscal year-end). Registered advisers must deliver the updated Form ADV Part 2A, or a summary of the changes made, to clients within 120 days following the adviser's fiscal year-end (by April 30, 2022 for advisers with a December 31 fiscal year-end). Although underlying investors of private funds managed by the advisers are not "clients" of the advisers under the Advisers Act, it is generally considered best practice to deliver the updated Form ADV Part 2A to these underlying investors on an annual basis.

In addition to the annual amendments, Form ADV Part 1 must be promptly amended where certain types of information reported, such as the disciplinary history of the investment adviser and/or its personnel, becomes inaccurate or, in certain cases, materially inaccurate. Form ADV Part 2A and Part 2B must be amended promptly whenever information reported becomes materially inaccurate. If the change relates to a disciplinary event, then the updated Form ADV Part 2A and/or Part 2B, as applicable, also must be delivered to clients. While Form ADV Part 2B is not required to be filed with the SEC, advisers must maintain copies in their records, and the Division of Examinations does ask for Part 2B when they do exams.

"Exempt reporting advisers" are subject to similar reporting requirements with respect to sections in Form ADV Part 1 that apply to them. If the exempt reporting adviser is exempt from SEC registration under the "private fund adviser" exemption, the exempt reporting adviser must register with the SEC once it reports in its annual amendment to Form ADV that its regulatory assets under management (RAUM) attributable to private funds have reached $150 million (or, in the case of an adviser based outside of the U.S., if the RAUM attributable to private fund assets managed at a place of business in the U.S. have reached $150 million). The exempt reporting adviser must apply for registration within 90 days of filing the amendment. If the exempt reporting adviser is exempt from SEC registration under the "venture capital fund adviser" exemption, the exempt reporting adviser must register with the SEC *prior* to the time it may no longer rely on such exemption.

Certain states impose "notice filing" requirements, requiring advisers to file their Form ADV with the relevant state securities authorities. Advisers may also be subject to additional state requirements where, for example, the adviser has a place of business in the state and/or has over five non-exempt clients in that state. Advisers may also be subject to certain blue sky requirements, as discussed below. An adviser should review its business on a periodic basis to determine whether any additional state requirements have been triggered.

Form PF

A registered adviser that advises one or more private funds and has at least $150 million in RAUM attributable to private funds is required to file Form PF with the SEC to report certain information regarding the private funds under its management. The frequency of the reporting obligation and the

amount of information that must be reported on Form PF will vary depending on the size of the adviser and the type of private funds managed by it.

In general, a registered adviser that has at least $150 million in RAUM attributable to private funds is required to file Form PF within 120 days after the end of the adviser's fiscal year (by April 30, 2022 for advisers with a December 31 fiscal year-end). However, the reporting requirements for advisers with larger RAUMs will be more frequent and/or more extensive. In particular:

- *Large Hedge Fund Advisers*. An adviser with at least $1.5 billion in RAUM attributable to hedge funds as of any month-end during the preceding fiscal quarter is subject to more comprehensive quarterly reporting requirements with respect to hedge funds under its management. In addition, the Large Hedge Fund Adviser is required to provide fund-specific information with respect to any "qualifying hedge funds" (*i.e.*, hedge funds with more than $500 million in net asset value). A Large Hedge Fund Adviser must file Form PF within 60 days of each quarter-end (by March 1, 2022 for the quarter ending December 31, 2021).
- *Large Private Equity Fund Advisers*. An adviser with at least $2.0 billion in RAUM attributable to private equity funds as of the end of the most recent fiscal year will be subject to more comprehensive annual reporting requirements with respect to private equity funds under its management. Large Private Equity Fund Advisers must file Form PF within 120 days of fiscal year-end (by April 30, 2022 for investment advisers with a December 31 fiscal year-end).
- *Large Liquidity Fund Advisers*. An adviser with at least $1.0 billion in RAUM attributable to private liquidity funds and registered money market funds as of any month-end during the preceding fiscal quarter will be subject to more comprehensive quarterly reporting requirements with respect to private liquidity funds under its management. Large Liquidity Fund Advisers must file Form PF within 15 days of each quarter-end (by January 15, 2022 for the quarter ending December 31, 2021).

For purposes of determining whether an adviser meets any of the large adviser classifications above, the adviser may disregard a private fund's equity investments in other private funds.

Exempt reporting advisers are not required to file Form PF.

Form D and Blue Sky Filings

Form D. A private fund conducting an offering under Rule 506 must file a Form D with the SEC on its filer management system, EDGAR, within 15 days of the initial sale of securities in such offering (*i.e.*, the date on which the first investor is irrevocably contractually committed to invest). For any ongoing offering for which a Form D was filed after March 16, 2009, Form D must be amended annually on or before the first anniversary of the last notice filed. Form D must also be amended as soon as practicable to correct a material mistake of fact or error or to reflect a change in the information provided in the previously filed notice. For certain specified types of changes in information, however, such as a change in the amount of securities sold in the offering or the number of investors who have invested in the offering, the private fund is not required to amend Form D until the next annual filing (if any) is due (but may choose to do so at any time).

Blue Sky Filings. Compliance with Rule 506 is very important for compliance with blue sky laws, since, under Section 18 of the Securities Act, the states are preempted from regulating offerings that comply with Rule 506. Without such compliance, unless an applicable self-executing state exemption is

available, a state where an investor purchases the issuer's securities can require a pre-sale filing and regulate the required disclosure and other aspects of the offering.

Provided that an offering is made in compliance with Rule 506, the blue sky laws of many states currently require that a hard copy of Form D be filed with the relevant state authority within 15 days following the initial sale of securities in that state, along with the state's required filing fee. In addition, some states' blue sky laws require that copies of amended SEC filings also be filed with the state. A handful of states require annual renewal filings and, in a couple of cases, the payment of annual renewal fees for ongoing offerings. Please note that the states now have a central electronic filing system for Rule 506 offerings, which is currently required to be used for filings in a few states, and possibly will be mandatory for all or most states in the not-too-distant future.

Advisers should be aware of requirements that may be triggered when sales of securities are made to investors in states where sales have not been made in the past, and sales in states in which a Form D has not yet been filed. The penalties for failing to make timely filings can be significant. Some states may require payment of a fine, or even demand that an issuer offer rescission to each investor in a state, or the administrator may issue a consent order.

Although Section 18 of the Securities Act states that covered securities, such as securities offered pursuant to Rule 506 of Regulation D, are not subject to state regulation, an increasing number of states have nevertheless used their authority under broker-dealer and investment adviser regulation and anti-fraud statutes to review and comment on Form Ds filed in connection with Rule 506 offerings. Questions regarding whether a related party listed under item 3 of the Form D is required to be registered as an investment adviser in the state are not unusual. Some states have also requested to see copies of the offering materials to be provided.

Form 13F

An adviser is required to file a Form 13F with the SEC if it exercises investment discretion over $100 million or more in Section 13(f) securities as of the last trading day of any month in any calendar year. In general, Section 13(f) securities include U.S.-listed equity securities, certain equity options and warrants, shares of closed-end investment companies and certain convertible debt securities. The SEC publishes an official list of Section 13(f) securities at the end of every quarter.

An adviser must file a Form 13F for the last quarter of the calendar year during which the reporting threshold is met. In addition, it must file a Form 13F for the first three quarters in the subsequent calendar year, even if its holding level has dropped below $100 million. In each case, Form 13F will be due within 45 days of quarter-end.

For advisers that exceeded the reporting threshold for the first time in 2021, the first Form 13F filing deadline in 2022 will be February 14, 2022 (for the quarter ending December 31, 2021).

Schedules 13D and 13G

A person that has direct or indirect beneficial ownership of more than 5% of a class of outstanding voting equity securities of a U.S. public company is required to file Schedule 13D, or Schedule 13G, if eligible, with the SEC. "Beneficial ownership" is defined to include the direct or indirect power to (i) vote the securities; or (ii) exercise investment authority over the securities, including the right to acquire the securities within 60 days (such as through the exercise of an option or a convertible security). Under this definition, "beneficial owners" may include a private fund, its investment adviser and certain controlling persons and/or parent companies of the adviser.

Schedule 13D. Schedule 13D must be filed within 10 days after crossing the 5% threshold and must be amended promptly following (i) a material increase or decrease in the filer's holding; or (ii) a material change in the Schedule 13D. An increase or decrease is deemed "material" if it equals at least 1% of the outstanding securities and may, depending on the facts and circumstances, be deemed "material" even if it is less than 1%.

Schedule 13G. A beneficial owner otherwise required to file Schedule 13D may file Schedule 13G if it acquired the securities in the ordinary course of its business and not with the purpose or effect of changing or influencing the control of the issuer.

> If the beneficial owner falls within any of the specified categories of "Qualified Institutional Investors" (QII), which includes SEC-registered investment advisers, it must file Schedule 13G within 45 days after the end of a calendar year if its holding crossed the 5% threshold during the year and is at least 5% as of year-end (by February 14, 2022 for 2021). Schedule 13G must be amended within 10 days of a month-end if the holding exceeds 10% of the class of equity securities as of such month-end and if it thereafter increases or decreases by more than 5% of the class of equity securities.
>
> A beneficial owner that does not qualify as a QII may still use Schedule 13G as a "passive investor," so long as its holding is below 20% of the class of securities. A passive investor must file Schedule 13G within 10 days of crossing the 5% threshold. Schedule 13G must be amended promptly once the holdings exceed 10% of the class of equity securities and if it thereafter increases or decreases by more than 5% of the class of equity securities.

Schedule 13G is also available to a beneficial owner that crossed the 5% threshold as of calendar year-end but is exempt from filing a Schedule 13D due to exemptions under Section 13(d) of the Exchange Act or otherwise. This may include, for example, a beneficial owner that met the 5% threshold at the time the issuer went public and continues to meet the 5% threshold at the end of the relevant calendar year-end, if other conditions are met. Each such exempt filer is required to file a Schedule 13G within 45 days after the end of a calendar year (by February 14, 2022 for 2021).

QII, passive investor and exempt investor filers must amend Schedule 13G within 45 days of each calendar year end to report any changes in the information previously reported, provided that no amendment will be required if the only change relates to the filer's percentage holding and is solely due to a change in the underlying aggregate number of outstanding shares in the class. The filing deadline for 2021 amendments will be February 14, 2022.

Forms 3, 4 and 5

Form 3. A person, including an adviser or other affiliate, depending on various factors, is required to file Form 3 with the SEC within 10 days of (i) acquiring beneficial ownership of more than 10% of a class of equity securities of a U.S. public company (including, among other things, puts, calls, options, warrants, convertible securities or other rights or obligations to buy or sell securities exercisable within 60 days); and/or (ii) becoming an officer or director of a U.S. public company. "Beneficial ownership" is defined in the same way as in the Schedule 13D and 13G context. With respect to an issuer undergoing an IPO, the initial Form 3 filing is due on the effective date of the registration.

Form 4. If a director, officer or 10% beneficial owner effects a transaction which changes the beneficial ownership of securities previously reported on Form 3, such director, officer or beneficial owner must file a Form 4 with the SEC within 2 business days of the transaction.

Form 5. Form 5 must be filed with the SEC within 45 days following the issuer's fiscal year end to report any exempt or other insider transactions not previously reported on Form 4 (by February 14, 2022 if the issuer has a fiscal year end of December 31).

Form 13H

Large traders of Regulation NMS securities (generally defined to be exchange-listed securities, including options) are required to file Form 13H with the SEC. A "large trader" is any person that exercises investment discretion over transactions in Regulation NMS securities that equal or exceed (i) two million shares or $20 million during any day; or (ii) 20 million shares or $200 million during any month. Large traders must file Form 13H with the SEC when the thresholds above are met. The initial Form 13H filing must be made "promptly" after reaching the threshold (generally within 10 days). Thereafter, an annual 13H filing must be submitted within 45 days of the end of the calendar year (by February 14, 2022 for 2021). Amendments to Form 13H must be filed promptly following the end of a calendar quarter if any information on the Form 13H becomes inaccurate. For example, the addition or removal of brokers would need to be reported at the end of a calendar quarter.

CFTC Annual Reaffirmations and Periodic Reports

CPO and CTA Exemption Reaffirmations. Each CPO exempt from CPO registration under CFTC Rule 4.5, 4.13(a)(1), 4.13(a)(2), 4.13(a)(3) or 4.13(a)(5) and each CTA exempt from CTA registration under CFTC Rule 4.14(a)(8) must submit an annual affirmation of its exemption via the NFA's Electronic Exemption System within 60 days of calendar year-end (by March 1, 2022 for 2022).

Annual Reports and Account Statement Requirements. Each registered CPO, including a CPO relying on CFTC Rule 4.7, must file financial statements of each commodity pool it operates with the NFA within 90 days after each such commodity pool's fiscal year-end (by March 31, 2022, if the fiscal year ends on December 31).

In addition, each registered CPO must distribute monthly account statements to participants of the commodity pool within 30 days of month-end for commodity pools with a net asset value greater than $500,000. For commodity pools with a net asset value of $500,000 or less, or operated under CFTC Rule 4.7, the CPO is instead required to distribute quarterly account statements to pool participants within 30 days of the quarter-end.

CFTC Form CPO-PQR and NFA Form PQR. Each registered CPO is required to report certain information to the CFTC on CFTC Form CPO-PQR. CFTC Form CPO-PQR contains three sections: Schedule A, Schedule B and Schedule C. The frequency that a CPO must file CFTC Form CPO-PQR and the sections that it must complete will depend on the CPO's amount of assets under management (AUM) and its SEC reporting obligations (if a dual registrant).

Each registered CPO that is an NFA member is also required to file NFA Form PQR quarterly with the NFA. NFA Form PQR consists of certain questions from Schedule A and Schedule B of CFTC Form CPO-PQR.

Both CFTC Form CPO-PQR and NFA Form PQR are filed on the NFA's EasyFile system. As NFA Form PQR is incorporated into CFTC Form CPO-PQR, there are no separate filings for the CFTC and the NFA. A CPO will satisfy its NFA Form PQR reporting obligations to the extent it is already responding to the same items on its CFTC Form CPO PQR for that reporting period.

In addition, CPOs that are registered as investment advisers with the SEC may satisfy certain of their CFTC Form CPO-PQR filing obligations by filing Form PF with the SEC.

Filing Requirements				
CPO Size	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Large CPO (CPO with AUM of at least $1.5 billion)	CFTC Form CPO-PQR Schedules A, B and C (within 60 days of quarter-end)	CFTC Form CPO-PQR Schedules A, B and C (within 60 days of quarter-end)	CFTC Form CPO-PQR Schedules A, B and C (within 60 days of quarter-end)	CFTC Form CPO-PQR Schedules A, B and C (within 60 days of quarter-end)
Mid-Sized CPO (CPO with AUM of at least $150 million but less than $1.5 billion)	NFA Form PQR (within 60 days of quarter-end)	NFA Form PQR (within 60 days of quarter-end)	NFA Form PQR (within 60 days of quarter-end)	CFTC Form CPO-PQR Schedules A and B (within 90 days of year-end)
Small CPO (CPO with AUM of less than $150 million)	NFA Form PQR (within 60 days of quarter-end)	NFA Form PQR (within 60 days of quarter-end)	NFA Form PQR (within 60 days of quarter-end)	CFTC Form CPO-PQR Schedule A and NFA Form PQR (within 90 days of year-end)
Dual-Registered CPO (CPO that is an SEC-registered investment adviser and files Form PF with the SEC)	NFA Form PQR (within 60 days of quarter-end)	NFA Form PQR (within 60 days of quarter-end)	NFA Form PQR (within 60 days of quarter-end)	CFTC Form CPO-PQR Schedule A and NFA Form PQR (within 60 or 90 days of quarter-end, depending on AUM)

The upcoming filing deadlines for the period ending on December 31, 2021 will be March 1, 2022 for Large CPOs and March 31, 2022 for Mid-Sized and Small CPOs.

CFTC Form CTA-PR and NFA Form PR. All registered CTAs, regardless of size and dual registration, must file CFTC Form CTA-PR annually within 45 days of the end of the fiscal year. CFTC Form CTA-PR covers certain identifying information about the CTA as well as performance information. In addition, each CTA that is an NFA member must file NFA Form CTA-PR within 45 days of each quarter-end. As the same form is used for CFTC Form CTA-PR and NFA Form PR, a CTA will satisfy its NFA Form PR obligation for the quarter ending on December 31 by filing its annual CFTC Form CTA-PR. Both CFTC Form CTA-PR and NFA Form PR are filed on the NFA's EasyFile system.

The deadline for the period ending December 31, 2021 will be February 14, 2022.

The CFTC has published a series of FAQs on CFTC Forms CPO-PQR and CTA-PR.

TIC Form B

A U.S. adviser (on behalf of itself and any U.S. or non-U.S. funds that it manages) and U.S. resident funds managed by a non-U.S. resident adviser are required to report cross-border claims, liabilities and short-term securities holdings on TIC B Forms with the Federal Reserve Bank of New York in each case if the reporting person is owed "reportable claims" or owes "reportable liabilities" in excess of certain monetary thresholds, as discussed below.

The TIC B Forms require reporting of current obligations (including loans, regardless of their maturity) and short term securities:

- that are owed by a U.S. resident entity to a non-U.S. resident, or by a non-U.S. resident entity to a U.S. resident;
- that are not held by a U.S. custodian or sub-custodian; and
- that are in excess of the relevant reporting thresholds (determined on an aggregated basis for the top-tier U.S. entity in an affiliated group, and separately for all of the funds that they manage).

TIC B Forms consist of a series of monthly and quarterly forms. Monthly TIC B filings (Forms BC, BL-1 and BL-2) are due no later than 15 days following the end of a month. Quarterly TIC B filings (Forms BQ-1, BQ-2 (Part 1), BQ-2 (Part 2) and BQ-3) are due no later than 20 days following the end of a quarter. If the due date of a report falls on a weekend or holiday, the due date is the following business day. Any financial institutions with "reportable claims" or "reportable liabilities" (as described below) exceeding the monetary thresholds and required to file for a reporting period are also required to file for all subsequent reporting periods in that year, regardless of whether the thresholds are exceeded in the subsequent periods. The reporting threshold for each TIC B Form (except Form BQ-3) is $50 million total ($25 million in any one foreign country). The reporting threshold for Form BQ-3 is $4 billion total (no country limit). A reporter is only required to file the applicable TIC B Forms for which its reportable claims and/or liabilities exceed the relevant threshold.

"Reportable claims" generally include all claims not held by a U.S. resident custodian or sub-custodian, including deposit balances due from banks, negotiable certificates of deposit of any maturity, brokerage balances, customer overdrawn accounts, loans and loan participations, resale agreements and similar financing agreements, short term (original maturity of one year or less) negotiable and non-negotiable securities, money-market instruments, reinsurance recoverables and accrued interest receivables.

"Reportable liabilities" generally include all liabilities not held by a U.S. resident custodian or sub-custodian, including non-negotiable deposits of any maturity, brokerage balances, overdrawn deposit accounts, loans of any maturity, short-term (original maturity of one year or less) non-negotiable securities, repurchase agreements and similar financing agreements, insurance technical reserves and accrued interest payables.

"Reportable claims" and "reportable liabilities" do not include long-term securities (including equities and any long-term notes, bonds and debentures), derivatives, credit commitments, contingent liabilities and securities borrowing or lending agreements in which one security is borrowed or lent in return for another. For purposes of the TIC B Forms, a feeder fund's investment into a master fund is considered a non-reportable long-term security and is not a reportable claim.

Representatives of the government agencies responsible for the TIC B Forms have indicated that any claims or liabilities held by a U.S. resident custodian or sub-custodian (such as a bank) or otherwise reportable by another U.S. financial institution (such as an administrative agent) should not be reported by investment advisers or funds, or be used to calculate whether the threshold limits have been exceeded.

A U.S. resident investment adviser reporting on behalf of itself and the entities in its organization should generally file Forms BC, BL-1, BQ-2 (Part 1) and/or BQ-3, as applicable. A U.S. resident investment adviser should generally file consolidated reports on behalf of the funds it manages, including reportable claims and liabilities of non-U.S. resident funds, on Forms BL-2, BQ-1 and BQ-2 (Part 2). Non-U.S. investment advisers do not have a reporting obligation, but any U.S. resident fund they manage may be required to make a TIC B filing.

TIC Form S

A U.S. resident entity, including a U.S. investment adviser, is required to file TIC Form S with the Federal Reserve Bank of New York if its transactions (*e.g.*, purchases, sales, redemptions and new issues) in long-term securities with foreign residents exceed $350 million in the aggregate during a month. Long-term securities are securities without a stated maturity date (such as equities) or with an original term-to-maturity of over a year.

Reportable transactions include, among other things, purchases and sales of newly-issued securities, purchases and sales of existing securities from other investors, and transactions resulting from sinking fund redemptions, called or maturing securities. Long-term securities received or delivered to settle derivative contracts are also reportable as purchases or sales by foreign residents. For U.S. investment advisers, reportable transactions include, among other things:

- purchases and sales they make for the accounts of their U.S. resident funds and other clients that are conducted directly with a foreign resident or placed through a foreign-resident broker, dealer or underwriter;
- purchases and sales made for the accounts of their foreign-resident funds and other clients that are placed through U.S. resident brokers, dealers or underwriters, if the identity of the underlying account holder had not been fully disclosed to such brokers, dealers or underwriters;
- redemptions from the accounts of their U.S. resident funds and other clients that are presented to a foreign resident intermediary (*e.g.*, a foreign-paying agent, foreign-resident broker, foreign-resident dealer or foreign-resident issuer) without the use of a U.S. resident custodian; and
- purchases and sales of interests in a foreign master fund by a U.S. resident feeder fund or in a U.S. resident master fund by a foreign feeder fund.

U.S. investment advisers meeting the reporting threshold in any given month must file TIC Form S no later than 15 days following month-end. If the due date of the report falls on a weekend or holiday, TIC Form S is due the following business day. U.S. investment advisers must continue to file TIC Form S monthly for the remainder of the calendar year, regardless of the level of transactions in the subsequent months.

TIC Form SLT

U.S. resident custodians (including U.S. resident banks), U.S. resident issuers (including U.S. private funds) and U.S. resident end-investors (including U.S. investment advisers, whether or not registered) are required to file TIC Form SLT with the Federal Reserve Bank of New York to report their cross-border ownership of reportable long term securities if the fair market value of their reportable holdings and issuances equals at least $1 billion as of the last business day of any month.

Most equity securities and debt securities with a maturity of greater than one year are considered reportable long term securities for purposes of Form SLT. Certain types of securities are excluded, such as, among other things, short-term securities (original maturity of one year or less), bankers' acceptances and trade acceptances, derivative contracts (including forward contracts to deliver securities), loans and loan participation certificates, letters of credit, bank deposits and annuities.

U.S. advisers with aggregate holdings of reportable long-term securities with a fair market value of at least $1 billion by the adviser and its clients are likely to be subject to Form SLT reporting. An adviser that is subject to the reporting requirement will file one consolidated report for all U.S. resident parts of its organization and all U.S. resident entities that it advises. Funds organized under the laws of any U.S. state are included in the "U.S. resident" portion of a reporting adviser's organization, which will subject securities issued by non-U.S. master funds that are held by U.S. feeder funds and holdings of U.S. master fund securities by non-U.S. feeder funds to reporting.

For U.S. resident holdings of non-U.S. securities, the reporting party would be required to disclose:

- the residence of the non-U.S. issuer; and
- the fair market value and type of non-U.S. security.

For non-U.S. resident holdings of U.S. securities, the reporting party would be required to disclose:

- the non-U.S. holder's residence;
- the fair market value and type of U.S. security; and
- whether the non-U.S. holder is a "foreign official institution" (including national governments, international and regional organizations and sovereign wealth funds).

Form SLT must be filed monthly by the 23rd day following the end of each month (*e.g.,* by January 23, 2022 for December 2021). If the due date of the report falls on a weekend or holiday, the TIC Form SLT report should be submitted the following business day. If the $1 billion threshold is crossed as of the end of any month, the reporting person must file Form SLT for all remaining months in that calendar year regardless of the subsequent amount of its reportable holdings.

BE-13

BE-13 collects data on new foreign direct investment in the U.S. from U.S. persons that meet the reporting requirements, even if such U.S. person has not been contacted by the BEA.

A U.S. entity is required to make a BE-13A filing if a non-U.S. person acquires direct or indirect ownership or control of 10% or more of the voting securities of such U.S. entity. A U.S. entity that crosses the 10% reporting threshold must file a Form BE-13A if the cost of acquiring or establishing such interest exceeds $3 million. However, U.S. private funds will not have to report on BE-13 unless a foreign person

acquires 10% or more of the voting interests in an operating company indirectly through the U.S. private fund.

A different BE-13 form is required depending on the type of event that has occurred (*e.g.*, formation, acquisition, merger or expansion). If the 10% reporting threshold is crossed but the cost of the transaction does not exceed $3 million, a U.S. entity must file a BE-13 Claim for Exemption. The BE-13 forms are due no later than 45 calendar days after an acquisition is completed, a new U.S. business enterprise is established, or the expansion is begun.

The discussion above focuses on the regulatory obligations applicable to investment advisers to private funds and the filing obligations applicable to other types of investment advisers (particularly investment advisers to separately management accounts or retail investors, banks, bank holding companies and non-financial entities) may be different.

Annual U.S. Tax Elections and Filings

This section briefly summarizes certain U.S. tax filings and elections (and related deadlines) relevant to private funds, their investors and related persons.

Form 8832 Filings. If an entity filed an IRS Form 8832 (an entity classification election) with respect to 2021, that entity must attach a copy of the Form 8832 with its U.S. federal income tax return. If that entity is not required to file a U.S. return, all direct or indirect owners of that entity generally must attach a copy with their U.S. federal income tax returns, if they are otherwise required to file U.S. returns. The deadline will be the due date (including any applicable extensions) of the filer's 2021 U.S. federal income tax return.

"Qualified Electing Fund" (QEF) Election. If a private fund has invested in a non-U.S. portfolio company that is (or may be) a "passive foreign investment company" (PFIC), the first U.S. person in the PFIC's ownership chain (*e.g.*, the fund itself, if a U.S. fund, or each U.S. investor, if a non-U.S. fund) may wish to file a QEF election with respect to that PFIC. The QEF election must be filed with that U.S. person's U.S. federal income tax return for the first year in which the fund invested in the PFIC. The deadline for PFICs acquired in 2021 will be the due date (including any applicable extensions) of that U.S. person's 2021 U.S. federal income tax return.

"Electing Investment Partnership" (EIP) Election. Private funds that satisfy certain requirements may opt out of otherwise mandatory tax basis adjustments (including those that may result from transfers of interests in a fund) by filing an EIP election. The EIP election must be filed with the private fund's U.S. federal income tax return for the first year in which the election is intended to apply. For funds wishing to be treated as EIPs with respect to 2020 (and subsequent years), the deadline will be the due date (including any applicable extensions) of the private fund's 2021 U.S. federal income tax return.

CbCR Reporting. A U.S. tax resident parent entity of a multinational enterprise (MNE) group that has revenues of $850 million or more during the taxable year must file IRS Form 8975 by the due date (including any applicable extensions) of its 2021 U.S. federal income tax return.

Certain U.S. Tax Filings with respect to Non-U.S. Entities. U.S. private funds and their U.S. investors may be required to make certain filings with respect to non-U.S. entities owned by the private fund. These filings may include, without limitation:

- IRS Form 5471 (with respect to certain non-U.S. corporations, including "controlled foreign corporations," owned by the private fund);

- IRS Form 926 (with respect to certain contributions of property to a non-U.S. corporation);
- IRS Form 8621 (with respect to certain non-U.S. corporations that are PFICs; however, such reporting generally is not required of U.S. tax-exempt investors);
- IRS Form 8865 (with respect to certain non-U.S. partnerships);
- IRS Form 8858 (with respect to certain non-U.S. disregarded entities);
- IRS Form 8938 (with respect to certain non-U.S. financial assets); and
- IRS Form 8992 (with respect to certain U.S. shareholders of controlled foreign corporations to calculate their share of "global intangible low-taxed income" (GILTI)).

Generally, the deadline will be the due date (including any applicable extensions) of the U.S. person's 2021 U.S. federal income tax return.

Other Annual Requirements and Considerations

Audited Financial Statements Delivery

Rule 206(4)-2 of the Advisers Act (the Custody Rule) requires registered advisers with custody of client assets to implement certain safeguards designed to protect client assets against the risk of loss, misuse or misappropriation. Among other things, it requires assets of an adviser's clients to be held by a qualified custodian and to be subject to surprise annual examinations by an independent public accountant that is registered with and subject to inspection by the Public Company Accounting Oversight Board (PCAOB). With respect to private fund clients, however, an adviser, rather than complying with the surprise audit requirement, may comply with the Custody Rule by relying on the Audit Provision under part (b)(4) of the Custody Rule. To rely on the Audit Provision, the adviser must have an independent public accountant that is registered with and subject to inspection by the PCAOB conduct an annual audit of each private fund client and deliver audited financial statements to all of its private fund investors. The audited financial statements must be delivered:

- within 120 days of the private fund's fiscal year-end (by April 30, 2022, if the fiscal year ends on December 31); or
- within 180 days of the private fund's fiscal year-end, if the private fund is a fund-of-funds (by June 29, 2022, if the fiscal year ends on December 31).

The accountant conducting the annual audit must be registered with and subject to inspection by the PCAOB. Currently, only auditors to public companies are subject to regular inspection by the PCAOB. However, on December 11, 2019, the staff of the SEC's Investment Adviser Regulation Office in the Division of Investment Management issued a no-action letter which affirmed continuing relief that the SEC would not recommend enforcement action against an adviser engaging an auditor that is not subject to inspection by the PCAOB to audit the financial statements of a pooled investment vehicle in connection with the annual audit provision, on the condition that such auditor was (i) registered with the PCAOB, and (ii) engaged to audit the financial statements of a broker or a dealer as of the commencement of the professional engagement period and as of each calendar-year end. This relief was permitted by the SEC through the date the SEC would approve a PCAOB-adopted permanent program for the inspection of broker and dealer auditors.

Privacy Policy Delivery

Following changes to the Gramm-Leach-Bliley Act contained in Section 75001 of the Fixing America's Surface Transportation Act of 2015 (the FAST Act), and subsequent 2019 conforming rulemaking from the CFTC, 2018 rule amendments from the U.S. Bureau of Consumer Financial Protection and 2019 staff guidance from the Division of Examinations, delivery of annual privacy notices is now required only if a financial institution's privacy policies and practices have changed since the last distribution of a privacy notice. Specifically, if there has been any change to the privacy policy that would permit non-public client information to be disclosed to non-affiliated third parties, and the new disclosure is not covered in the existing notice, the financial institution must deliver an updated notice to clients and provide them a reasonable opportunity to opt out of the new disclosure.

Schedule K-1 Delivery

Under IRS rules, partnerships are required to deliver certain information on Schedule K-1 to their partners on or before the day on which the return for the relevant taxable year is required to be filed. As required by IRS rules issued in 2012, a partnership must obtain a partner's affirmative consent for the partnership to validly deliver Schedule K-1 to the partner electronically (*e.g.*, via email or by posting the Schedule K-1 on a web portal). For the consent to be valid, it must be obtained from a partner in the same electronic manner in which the partnership will deliver the Schedule K-1 to the partner. The applicable IRS rules also prescribe certain other requirements for electronic delivery of Schedule K-1s, including certain disclosures, which must be provided to partners regarding electronic delivery of Schedule K-1s. In addition to these IRS rules, states or other jurisdictions may impose security requirements for maintenance and transmission of sensitive personal information (such as individual Social Security numbers), which a partnership may need to comply with when delivering Schedule K-1s to its partners.

New Issues Investor Reaffirmations

If a private fund intends to invest in "new issues," the adviser will often obtain annual reaffirmations from the private fund's investors relating to each such investor's eligibility to participate in profits and losses from new issues. Reaffirmation may be obtained by sending out notices asking each investor to notify the adviser if the investor's new issues status has changed or by including a representation in the investor's subscription agreement whereby the investor agrees to notify the adviser of any subsequent change in its new issues status.

ERISA/VCOC Annual Certifications and Compliance

Many private funds that accept investments from investors subject to ERISA are operated in such a manner so that the assets of such private funds do not constitute the "plan assets" of ERISA investors for purposes of ERISA. Typically, such a fund will either be operated as a "venture capital operating company" (VCOC) or so that "benefit plan investor" equity participation is not "significant" (*i.e.*, under the ERISA 25% limit), and the sponsor of such a private fund often will contractually agree with its ERISA investors to deliver an annual certification as to the private fund's continued compliance with the VCOC requirements and/or the 25% benefit plan investor limit. Private funds that accept investments from ERISA investors should conduct the VCOC or 25% benefit plan investor limit analysis as applicable, whether or not they are required to annually certify compliance with respect thereto, and should be prepared to deliver any required or requested certifications in a timely manner.

Private funds that are designed to hold "plan assets" and that actually are holding "plan assets" of ERISA investors may need to provide the ERISA investors with certain information (sometimes referred to as

"408(b)(2) disclosures," by reference to the relevant section of ERISA) relating to any changes to the fees or expenses paid by the fund and/or certain other information relating to the fund manager's compensation that is requested by an ERISA investor and required for the ERISA investor's compliance with its reporting and disclosure obligations under ERISA.

California Financing Law Requirements

The California Financing Law generally requires lenders (including private funds) "engaged in the business of a finance lender" in California to obtain a license, although there is an exemption for a person making no more than five loans per year, so long as the loans are incidental to the business of the person relying on the exemption (*e.g.*, bridge loans to a portfolio company) and the person is not engaged in the business of making loans. The licensing process is cumbersome and time-consuming, but willful violation of the law can result in civil and criminal penalties. A license holder is subject to certain inspection and reporting obligations.

Lobbyist Registration

Under a California law that became effective January 1, 2011, "placement agents" hired or engaged to solicit California state plans (*e.g.*, CalSTRS, CalPERS and the University of California pension system) are required to register as lobbyists. Under existing law, lobbyists are restricted in their ability to provide gifts and make campaign contributions and are prohibited from accepting fees contingent upon the success of their lobbying efforts. Under the 2011 law, certain employees of a fund sponsor may be subject to the lobbyist registration requirements and the gift and campaign contribution limits, and sponsors that retain placement agents may have filing and record keeping obligations as "lobbyist employers." Any party contemplating retention of a placement agent or any solicitation of CalSTRS, CalPERS or the University of California pension system can contact a member of Proskauer for more information.

In addition, under New York City's Lobbying Law and based on regulatory guidance issued in 2010-2012, placement agents and/or employees of investment advisers may be required to register with New York City in connection with the offering of fund interests to any of the New York City pension funds (including New York City Employees' Retirement System, the New York City Police Pension Fund, the New York Fire Department Pension Fund, the New York City Teachers' Retirement System, and the New York City Board of Education Retirement System). Although the Lobbying Law had been in effect for 20 years, it had not been previously interpreted to apply to the marketing activities of investment funds and their agents.

As a reminder, other state and local plans have their own regulations and policies on the use of placement agents (including disclosure or placement agent bans in some circumstances), and lobbyist registration may be relevant for marketing to other state or local plans.

Liability Insurance

Investment advisers should consider purchasing management liability insurance depending on their level of exposure and the extent to which their business and operations warrant such coverage. Given the heightened regulatory scrutiny of the private funds industry, investment advisers may benefit from protection against officer and director liability, fiduciary liability, error and omission liability and employment practice liability.

2021 - 2022 Federal Filings and Other Document Delivery Calendar

Filing / Delivery	Who must file	Deadline
December 2021		
TIC Form BC, BL-1 and BL-2	U.S. residents with reportable cross-border claims or liabilities in excess of $50 million (or $25 million with respect to an individual country)	December 15 (for November 2021)
TIC Form S	U.S. resident entities conducting cross-border reportable transactions exceeding $350 million as of any month	December 15 (for November 2021)
TIC Form SLT	U.S. resident custodian, issuer or end-investor having cross-border ownership of reportable long-term securities exceeding $1 billion as of the last day of any calendar month	December 23 (for November 2021)
Delivery of Monthly Account Statements to Pool Participants	Registered CPOs (except for CPOs exempt under CFTC Reg. 4.7 or with respect to commodity pools with NAV below $500,000)	December 30 (for November 2021)
January 2022		
Form PF	Large Liquidity Fund Advisers	January 15 (for the quarter ending December 31, 2021)
TIC Form S	U.S. resident entities conducting cross-border reportable transactions exceeding $350 million as of any month	January 18 (for December 2021) Note: Usually filed 15 calendar days following the last business day of the month, but if the 15th day is a holiday, Saturday or Sunday, the filing deadline is extended until the next business day.
TIC Form BC, BL-1 and BL-2	U.S. residents with reportable cross-border claims or liabilities in excess of $50 million (or $25 million with respect to an individual country)	January 18 (for December 2021) Note: Usually filed on the 15th calendar day of the following month, but if the 15th day is a holiday, Saturday or Sunday, the filing deadline is extended until the next business day.

Filing / Delivery	Who must file	Deadline
TIC Form BQ-1, BQ-2 and BQ-3	U.S. residents with reportable cross-border claims or liabilities in excess of $50 million (or $25 million with respect to an individual country) (Form BQ-1 and BQ-2 Part 1), in excess of $50 million (no country limit) (Form BQ-2 Part 2) or in excess of $4 billion (no country limit) (Form BQ-3)	January 20 (for the quarter ending December 31, 2021)
TIC Form SLT	U.S. resident custodian, issuer or end-investor having cross-border ownership of reportable long-term securities exceeding $1 billion as of the last day of any calendar month	January 24 (for December 2021) Note: Usually filed on the 23rd calendar day of the following month, but if the 23rd day is a holiday, Saturday or Sunday, the filing deadline is extended until the next business day.
Delivery of Quarterly Account Statements to Pool Participants	Registered CPOs exempt under CFTC Reg. 4.7 or with respect to commodity pools with NAV below $500,000	January 30 (for the quarter ending December 31, 2021)
Delivery of Monthly Account Statements to Pool Participants	Registered CPOs (except for CPOs exempt under CFTC Reg. 4.7 or with respect to commodity pools with NAV below $500,000)	January 30 (for December 2021)
February 2022		
Schedule 13G Annual Amendment	Beneficial owners of at least 5% of a class of outstanding equity securities of a U.S. public company eligible to file Schedule 13G (*e.g.*, Qualified Institutional Investors and/or passive investors)	February 14 (for 2021)
Form 13H Annual Update	Large traders of Regulation NMS securities	February 14 (for 2021)
Form 5	Insiders required to report any exempt or other insider transactions not previously reported on Form 4	February 14 (if the issuer has a December 31 fiscal year-end)
CFTC Form CTA-PR	Registered CTAs	February 14 (for the quarter ending December 31, 2021)

Filing / Delivery	Who must file	Deadline
Form 13F	Investment managers that exercise investment discretion over $100 million or more in Section 13(f) securities	February 14 (for the quarter ending December 31, 2021)
TIC Form BC, BL-1 and BL-2	U.S. residents with reportable cross-border claims or liabilities in excess of $50 million (or $25 million with respect to an individual country)	February 15 (for January 2022)
TIC Form S	U.S. resident entities conducting cross-border reportable transactions exceeding $350 million as of any month	February 15 (for January 2022)
TIC Form SLT	U.S. resident custodian, issuer or end-investor having cross-border ownership of reportable long-term securities exceeding $1 billion as of the last day of any calendar month	February 23 (for January 2022)
March 2022		
Form PF	Large Hedge Fund Advisers	March 1 (for the quarter ending December 31, 2021)
CFTC Form CPO-PQR	Large CPOs	March 1 (for the quarter ending December 31, 2021)
CFTC Registration Exemption Reaffirmations	CPOs exempt from CPO registration under CFTC Rule 4.5, 4.13(a)(1), 4.13(a)(2), 4.13(a)(3) or 4.13(a)(5) and CTAs exempt from CTA registration under CFTC Rule 4.14(a)(8)	March 1 (for 2021)
Delivery of Monthly Account Statements to Pool Participants	Registered CPOs (except for CPOs exempt under CFTC Reg. 4.7 or with respect to commodity pools with NAV below $500,000)	March 2 (for January 2022)
TIC Form BC, BL-1 and BL-2	U.S. residents with reportable cross-border claims or liabilities in excess of $50 million (or $25 million with respect to an individual country)	March 15 (for February 2022)

Filing / Delivery	Who must file	Deadline
TIC Form S	U.S. resident entities conducting cross-border reportable transactions exceeding $350 million as of any month	March 15 (for February 2022)
TIC Form SLT	U.S. resident custodian, issuer or end-investor having cross-border ownership of reportable long-term securities exceeding $1 billion as of the last day of any calendar month	March 23 (for February 2022)
Delivery of Monthly Account Statements to Pool Participants	Registered CPOs (except for CPOs exempt under CFTC Reg. 4.7 or with respect to commodity pools with NAV below $500,000)	March 30 (for February 2022)
CRS Information Reports	Financial institutions in "Participating Jurisdictions" (which currently do not include the US)	Consult local advisers
Form ADV Annual Update	Registered investment advisers and exempt reporting advisers	March 31 (for an investment adviser with a December 31 fiscal year-end)
NFA Commodity Pool Annual Financial Statements Filing	Registered CPOs	March 31 (for a pool with a December 31 fiscal year-end)
FATCA Information Report	Participating FFIs (except for FFIs in Model 1 IGA jurisdictions) FFIs in Model 1 IGA jurisdictions	Consult local advisers
April 2022		
FBAR	Hedge funds and private equity funds, and their investment advisers, if they have non-U.S. bank or other financial accounts	April 15 (with a six-month extension available upon request)
Form PF	Large Liquidity Fund Advisers	April 15 (for the quarter ending March 31, 2022)
TIC Form BC, BL-1 and BL-2	U.S. residents with reportable cross-border claims or liabilities in excess of $50 million (or $25 million with respect to an individual country)	April 15 (for March 2022)

Filing / Delivery	Who must file	Deadline
TIC Form S	U.S. resident entities conducting cross-border reportable transactions exceeding $350 million as of any month	April 15 (for March 2022)
TIC Form BQ-1, BQ-2 and BQ-3	U.S. residents with reportable cross-border claims or liabilities in excess of $50 million (or $25 million with respect to an individual country) (Form BQ-1 and BQ-2 Part 1), in excess of $50 million (no country limit) (Form BQ-2 Part 2), or in excess of $4 billion (no country-limit) (Form BQ-3)	April 20 (for the quarter ending March 31, 2022)
TIC Form SLT	U.S. resident custodian, issuer or end-investor having cross-border ownership of reportable long-term securities exceeding $1 billion as of the last day of any calendar month	April 25 (for March 2022) Note: Usually filed on the 23rd calendar day of the following month, but if the 23rd day is a holiday, Saturday or Sunday, the filing deadline is extended until the next business day.
Form PF	Registered investment advisers with at least $150 million in RAUM attributable to private funds, including Large Private Equity Fund Advisers	April 30 (for an investment adviser with a December 31 fiscal year-end)
Delivery of Annual Audited Financial Statements to Private Fund Investors	Registered investment advisers (except with respect to fund-of-funds)	April 30 (for private fund with a December 31 fiscal year-end)
Delivery of Monthly Account Statements to Pool Participants	Registered CPOs (except for CPOs exempt under CFTC Reg. 4.7 or with respect to commodity pools with NAV below $500,000)	April 30 (for March 2022)
Delivery of Quarterly Account Statements to Pool Participants	Registered CPOs exempt under CFTC Reg. 4.7 or with respect to commodity pools with NAV below $500,000	April 30 (for March 2022)
Delivery of Updated Form ADV Part 2A to Clients	Registered investment advisers	April 30 (for an investment adviser with a December 31 fiscal year end)
May 2022		

Filing / Delivery	Who must file	Deadline
NFA Form PR	All registered CTAs	May 15 (for the quarter ending March 31, 2022)
Form 13F	Investment managers that exercise investment discretion over $100 million or more in Section 13(f) securities	May 16 (for the quarter ending March 31, 2022) Note: Usually filed 45 days after quarter end, but if the day is a holiday, Saturday or Sunday, the filing deadline is extended until the next business day.
TIC Form BC, BL-1 and BL-2	U.S. residents with reportable cross-border claims or liabilities in excess of $50 million (or $25 million with respect to an individual country)	May 16 (for April 2022) Note: Usually filed on the 15th calendar day of the following month, but if the 15th day is a holiday, Saturday or Sunday, the filing deadline is extended until the next business day.
TIC Form S	U.S. resident entities conducting cross-border reportable transactions exceeding $350 million as of any month	May 16 (for April 2022) Note: Usually filed 15 calendar days following the last business day of the month, but if the 15th day is a holiday, Saturday or Sunday, the filing deadline is extended until the next business day.
TIC Form SLT	U.S. resident custodian, issuer or end-investor having cross-border ownership of reportable long-term securities exceeding $1 billion as of the last day of any calendar month	May 23 (for April 2022)
Form PF	Large Hedge Fund Advisers	May 30 (for the quarter ending March 31, 2022)
CFTC Form CPO-PQR	Large CPOs	May 31 (for the quarter ending March 31, 2022) Note: Usually filed within 60 days of each calendar quarter end, but if the day is a holiday, Saturday or Sunday, the filing deadline is extended until the next business day.

Filing / Delivery	Who must file	Deadline
NFA Form CPO-PQR	All registered CPOs, except Large CPOs	May 31 (for the quarter ending March 31, 2022) Note: Usually filed within 60 days of each calendar quarter end, but if the day is a holiday, Saturday or Sunday, the filing deadline is extended until the next business day.
Delivery of Monthly Account Statements to Pool Participants	Registered CPOs (except for CPOs exempt under CFTC Reg. 4.7 or with respect to commodity pools with NAV below $500,000)	May 30 (for April 2022)
June 2022		
TIC Form BC, BL-1 and BL-2	U.S. residents with reportable cross-border claims or liabilities in excess of $50 million (or $25 million with respect to an individual country)	June 15 (for May 2022)
TIC Form S	U.S. resident entities conducting cross-border reportable transactions exceeding $350 million as of any month	June 15 (for May 2022)
TIC Form SLT	U.S. resident custodian, issuer or end-investor having cross-border ownership of reportable long-term securities exceeding $1 billion as of the last day of any calendar month	June 23 (for May 2022)
Delivery of Annual Audited Financial Statements to Private Fund Investors	Registered investment advisers (with respect to fund-of-funds)	June 29 (for a fund-of-funds with a December 31 fiscal year-end)
Delivery of Monthly Account Statements to Pool Participants	Registered CPOs (except for CPOs exempt under CFTC Reg. 4.7 or with respect to commodity pools with NAV below $500,000)	June 30 (for May 2022)
July 2022		
Form PF	Large Liquidity Fund Advisers	July 15 (for the quarter ending June 30, 2022)

Filing / Delivery	Who must file	Deadline
TIC Form BC, BL-1 and BL-2	U.S. residents with reportable cross-border claims or liabilities in excess of $50 million (or $25 million with respect to an individual country)	July 15 (for June 2022)
TIC Form S	U.S. resident entities conducting cross-border reportable transactions exceeding $350 million as of any month	July 15 (for June 2022)
TIC Form BQ-1, BQ-2 and BQ-3	U.S. residents with reportable cross-border claims or liabilities in excess of $50 million (or $25 million with respect to an individual country) (Form BQ-1 and BQ-2 Part 1), in excess of $50 million (no country-limit) (Form BQ-2 Part 2), or in excess of $4 billion (no country-limit) (Form BQ-3)	July 20 (for the quarter ending June 30, 2022)
TIC Form SLT	U.S. resident custodian, issuer or end-investor having cross-border ownership of reportable long-term securities exceeding $1 billion as of the last day of any calendar month	July 25 (for June 2022) Note: Usually filed on the 23rd calendar day of the following month, but if the 23rd day is a holiday, Saturday or Sunday, the filing deadline is extended until the next business day.
Delivery of Quarterly Account Statements to Pool Participants	Registered CPOs exempt under CFTC Reg. 4.7 or with respect to commodity pools with NAV below $500,000	July 30 (for the quarter ending June 30, 2022)
Delivery of Monthly Account Statements to Pool Participants	Registered CPOs (except for CPOs exempt under CFTC Reg. 4.7 or with respect to commodity pools with NAV below $500,000)	July 30 (for June 2022)
August 2022		
NFA Form PR	All registered CTAs	August 14 (for the quarter ending June 30, 2022)

Filing / Delivery	Who must file	Deadline
Form 13F	Investment managers that exercise investment discretion over $100 million or more in Section 13(f) securities	August 15 (for the quarter ending June 30, 2022) Note: Usually filed 45 days after previous quarter end, but if the day is a holiday, Saturday or Sunday, the filing deadline is extended until the next business day.
TIC Form BC, BL-1 and BL-2	U.S. residents with reportable cross-border claims or liabilities in excess of $50 million (or $25 million with respect to an individual country)	August 15 (for July 2022)
TIC Form S	U.S. resident entities conducting cross-border reportable transactions exceeding $350 million as of any month	August 15 (for July 2022)
TIC Form SLT	U.S. resident custodian, issuer or end-investor having cross-border ownership of reportable long-term securities exceeding $1 billion as of the last day of any calendar month	August 23 (for July 2022)
Form PF	Large Hedge Fund Advisers	August 29 (for the quarter ending June 30, 2022)
CFTC Form CPO-PQR	Large CPOs	August 29 (for the quarter ending June 30, 2022)
NFA Form CPO-PQR	All registered CPOs, except Large CPOs	August 29 (for the quarter ending June 30, 2022)
Delivery of Monthly Account Statements to Pool Participants	Registered CPOs (except for CPOs exempt under CFTC Reg. 4.7 or with respect to commodity pools with NAV below $500,000)	August 30 (for July 2022)
September 2022		
TIC Form BC, BL-1 and BL-2	U.S. residents with reportable cross-border claims or liabilities in excess of $50 million (or $25 million with respect to an individual country)	September 15 (for August 2022).

Filing / Delivery	Who must file	Deadline
TIC Form S	U.S. resident entities conducting cross-border reportable transactions exceeding May $350 million as of any month	September 15 (for August 2022)
TIC Form SLT	U.S. resident custodian, issuer or end-investor having cross-border ownership of reportable long-term securities exceeding $1 billion as of the last day of any calendar month	September 23 (for August 2022)
Delivery of Monthly Account Statements to Pool Participants	Registered CPOs (except for CPOs exempt under CFTC Reg. 4.7 or with respect to commodity pools with NAV below $500,000)	September 30 (for August 2022)
October 2022		
Form PF	Large Liquidity Fund Advisers	October 15 (for the quarter ending September 30, 2022)
TIC Form S	U.S. resident entities conducting cross-border reportable transactions exceeding $350 million as of any month	October 17 (for September 2022) Note: Usually filed 15 calendar days following the last business day of the month, but if the 15th day is a holiday, Saturday or Sunday, the filing deadline is extended until the next business day.
TIC Form BC, BL-1 and BL-2	U.S. residents with reportable cross-border claims or liabilities in excess of $50 million (or $25 million with respect to an individual country)	October 17 (for September 2022) Note: Usually filed 15 days after previous month end, but if the day is a holiday, Saturday or Sunday, the filing deadline is extended until the next business day.
TIC Form BQ-1, BQ-2 and BQ-3	U.S. residents with reportable cross-border claims or liabilities in excess of $50 million (or $25 million with respect to an individual country) (Form BQ-1 and BQ-2 Part 1), in excess of $50 million (no country limit) (Form BQ-2 Part 2), or in excess of $4 billion (no country limit) (Form BQ-3)	October 20 (for the quarter ending September 30, 2022)

Filing / Delivery	Who must file	Deadline
TIC Form SLT	U.S. resident custodian, issuer or end-investor having cross-border ownership of reportable long-term securities exceeding $1 billion as of the last day of any calendar month	October 24 (for September 2022) Note: Usually filed on the 23rd calendar day of the following month, but if the 23rd day is a holiday, Saturday or Sunday, the filing deadline is extended until the next business day.
Delivery of Quarterly Account Statements to Pool Participants	Registered CPOs exempt under CFTC Reg. 4.7 or with respect to commodity pools with NAV below $500,000	October 30 (for the quarter ending September 30, 2022)
Delivery of Monthly Account Statements to Pool Participants	Registered CPOs (except for CPOs exempt under CFTC Reg. 4.7 or with respect to commodity pools with NAV below $500,000)	October 30 (for September 2022)
November 2022		
NFA Form PR	All registered CTAs	November 14 (for the quarter ending September 30, 2022)
Form 13F	Investment managers that exercise investment discretion over $100 million or more in Section 13(f) securities	November 14 (for the quarter ending September 30, 2022)
TIC Form BC, BL-1 and BL-2	U.S. residents with reportable cross-border claims or liabilities in excess of $50 million (or $25 million with respect to an individual country)	November 15 (for October 2022)
TIC Form S	U.S. resident entities conducting cross-border reportable transactions exceeding $350 million as of any month	November 15 (for October 2022)
TIC Form SLT	U.S. resident custodian, issuer or end-investor having cross-border ownership of reportable long-term securities exceeding $1 billion as of the last day of any calendar month	November 23 (for October 2022)
Form PF	Large Hedge Fund Advisers	November 29 (for the quarter ending September 30, 2022)

Filing / Delivery	Who must file	Deadline
CFTC Form CPO-PQR	Large CPOs	November 29 (for the quarter ending September 30, 2022)
NFA Form CPO-PQR	All registered CPOs, except Large CPOs	November 30 (for the quarter ending September 30, 2022)
Delivery of Monthly Account Statements to Pool Participants	Registered CPOs (except for CPOs exempt under CFTC Reg. 4.7 or with respect to commodity pools with NAV below $500,000)	November 30 (for October 2022)
Other Floating Deadlines		
Form D	Private funds conducting an offering under Regulation D	Initial Filing: Within 15 days of the initial sale of securities Annual Amendment: Anniversary date of the previous Form D filing Interim Amendment: As soon as practicable after certain changes in information Note: Additional state blue sky filing requirements may apply
Schedule 13D	Beneficial owners of at least 5% of a class of outstanding equity securities of a U.S. public company	Initial Filing: Within 10 days of crossing the 5% threshold Amendment: Promptly after any material change in beneficial ownership percentage

Filing / Delivery	Who must file	Deadline
Schedule 13G	Beneficial owners of at least 5% of a class of outstanding equity securities of a U.S. public company eligible to file Schedule 13G (*i.e.*, Qualified Institutional Investors and/or passive investors)	Initial Filing: Generally, within 45 days of year-end (if a QII or passive investor) or within 10 days of crossing the 5% threshold (if a passive investor) Annual Amendment: Within 45 days of year-end (see above) Interim Amendment: Within 10 days of month-end (if a QII) or promptly (if a passive investor) if holding exceeds 10% or if it thereafter increases or decreases by over 5%
Form 13H	Large traders of Regulation NMS securities	Initial Filing: Promptly (usually 10 days) after reaching reporting threshold Annual Amendment: Within 45 days of year-end (see above) Interim Amendment: Promptly after quarter-end if there is any change in information
Form 3	Beneficial owners of more than 10% of a class of equity securities of a U.S. public company, or officers or directors of a U.S. public company	Within 10 days of becoming a 10% beneficial owner, officer or director
Form 4	Beneficial owners of more than 10% of a class of equity securities of a U.S. public company or officers or directors of a U.S. public company that effect a transaction changing the beneficial ownership of securities previously reported on Form 3	Within 2 business days of the transaction

Filing / Delivery	Who must file	Deadline
Hart-Scott-Rodino Filings	Persons contemplating a business transaction which is not "solely for the purpose of investment" and relates to either: (i) the acquisition of voting securities valued in excess of $84.4 million (adjusted annually); or (ii) the acquisition of a majority of interests in certain unincorporated entities (such as certain partnerships or LLCs). The passive investor exemption is available only for holdings not exceeding 10% of an issuer's voting stock	Prior to completion of the proposed business transaction Note: Filers are generally subject to 30-day waiting period after submitting their HSR notice filing
Form BE-13A or BE-13 Claim for Exemption	U.S. entities in which a non-U.S. person acquires direct or indirect ownership or control of 10% or more of the voting securities If the cost of the transaction exceeds $3 million, then the U.S. entity should file Form BE-13A If the cost of the transaction does not exceed $3 million, then the U.S. entity should file a BE-13 Claim for Exemption	Within 45 days after a reportable transaction
New Issues Affirmations	Private funds that invest in new issues	Annually
Delivery of Privacy Policy Notice to Clients	Financial institutions who have changed their privacy policies and practices since the last distribution of a privacy notice (see above)	Annually
Delivery of ERISA/VCOC Annual Certification to ERISA Investors	Private funds operating as a VCOC or pursuant to the 25% cap	As per fund documents and/or other contractual agreements with ERISA investors (typically no more frequently than annually)
Delivery of Schedule K-1	Private funds that are partnerships for tax purposes	Due date (including any applicable extension) of the partnership's U.S. federal income tax return

Filing / Delivery	Who must file	Deadline
Form 8832 Filing	Entities that filed an IRS Form 8832 with respect to 2021	Due date (including any applicable extension) of that entity's 2021 U.S. federal income tax return
QEF Election	In the case of a private fund that has invested in a non-U.S. portfolio company that is (or may be) a PFIC, the first U.S. person in the PFIC's ownership chain (*e.g.*, the fund itself if a U.S. fund, or each U.S. investor if a non-U.S. fund)	Due date (including any applicable extensions) of that U.S. person's 2021 U.S. federal income tax return
EIP Election	Eligible private funds wishing to opt out of mandatory tax basis adjustments	Due date (including any applicable extensions) of that private fund's 2021 U.S. federal income tax return
CbCR – Form 8975	U.S. tax resident parent entity of a MNE that has revenues of $850 million or more during the taxable year	Due date (including any applicable extension) of that entity's 2021 U.S. federal income tax return
Certain U.S. Tax Filings with respect to Non-U.S. Entities	Private funds and their U.S. investors may be required to make certain filings with respect to non-U.S. entities owned by the private fund, including, without limitation: IRS Form 5471 IRS Form 926 IRS Form 8621 IRS Form 8865 IRS Form 8858 IRS Form 8938	Generally, due date (including any applicable extensions) of the U.S. person's 2021 U.S. federal income tax return

Contacts

For additional information on matters discussed in this Annual Review, please contact any of the Proskauer attorneys listed below:

HEDGE FUNDS

Caryn J. Greenspan
212.969.3281
cgreenspan@proskauer.com

Robert G. Leonard
212.969.3355
rleonard@proskauer.com

Michael F. Mavrides
212.969.3670
mmavrides@proskauer.com

Christopher M. Wells
212.969.3600
cwells@proskauer.com

Kelli L. Moll
212.969.3520
kmoll@proskauer.com

PRIVATE INVESTMENT FUNDS

Warren Allan
44.20.7280.2234
wallan@proskauer.com

Monica Arora
212.969.3003
marora@proskauer.com

Howard J. Beber
617.526.9754
hbeber@proskauer.com

Bruno Bertrand-Delfau
44.20.7280.2126
bbertrand-delfau@proskauer.com

Sarah K. Cherry
617.526.9769
scherry@proskauer.com

Niamh A. Curry
212.969.3474
ncurry@proskauer.com

Camille Higonnet
617.526.9738
chigonnet@proskauer.com

Jordan Hurwitz
44.20.7280.2083
jhurwitz@proskauer.com

David T. Jones
617.526.9751
djones@proskauer.com

Joseph E. Kasegian
617.526.9449
jkasegian@proskauer.com

Kirsten Lapham
44.20.7280.2031
klapham@proskauer.com

Edward Lee
44.20.7280.2057
etlee@proskauer.com

Galen R. Lewis
1.617.526.9405
glewis@proskauer.com

Stephen T. Mears
617.526.9775
smears@proskauer.com

Don B. Melamed
310.284.5621
dmelamed@proskauer.com

Kelli L. Moll
212.969.3520
kmoll@proskauer.com

Nicholas C. Noon
617.526.9490
nnoon@proskauer.com

Peter J. Olds
44.20.7280.2270
polds@proskauer.com

Robin A. Painter
617.526.9790
rpainter@proskauer.com

Charles (Chip) Parsons
212.969.3254
cparsons@proskauer.com

Marc A. Persily
212.969.3403
mpersily@proskauer.com

Aranpreet Randhawa
44.20.7280.2235
arandhawa@proskauer.com

Yong Ren
86.10.8572.1899
yren@proskauer.com

Christopher C. Robinson
212.969.3676
ccrobinson@proskauer.com

Brian S. Schwartz
617.526.9785
bschwartz@proskauer.com

Kerry F. Shriver
617.526.9413
kshriver@proskauer.com

Michael R. Suppappola
617.526.9821
msuppappola@proskauer.com

David W. Tegeler
617.526.9795
dtegeler@proskauer.com

Nigel van Zyl
44.20.7280.2070
nvanzyl@proskauer.com

John Verwey
44.20.7280.2033
jverwey@proskauer.com

Fabio A. Yamada
55.11.3045.1250
fyamada@proskauer.com

REGISTERED FUNDS

Stuart H. Coleman
+1.212.969.3350
scoleman@proskauer.com

Bradford A. Green
212.969.3359
bgreen@proskauer.com

Janna Manes
+1.212.969.3363
jmanes@proskauer.com

Robert E. Plaze
+1.202.416.6692
rplaze@proskauer.com

Nicole M. Runyan
+1.212.969.3361
nrunyan@proskauer.com

David Stephens
+1.212.969.3357
dstephens@proskauer.com

TAX

Richard M. Corn
212.969.3553
rcorn@proskauer.com

Michael Fernhoff
310.284.5671
mfernhoff@proskauer.com

Robert E. Gaut
44.20.7280.2064
rgaut@proskauer.com

Martin T. Hamilton
212.969.3964
mhamilton@proskauer.com

Scott S. Jones
617.526.9772
sjones@proskauer.com

Mary B. Kuusisto
44.20.7280.2159
mkuusisto@proskauer.com

Arnold P. May
617.526.9757
amay@proskauer.com

David S. Miller
212.969.3006
dmiller@proskauer.com

Jeremy M. Naylor
617.526.9441
jnaylor@proskauer.com

Amanda H. Nussbaum
212.969.3642
anussbaum@proskauer.com

Janicelynn Asamoto Park
212.969.3152
jpark@proskauer.com

Stephen Pevsner
44.20.7280.2041
spevsner@proskauer.com

Jamiel E. Poindexter
617.526.9773
jpoindexter@proskauer.com

Catherine Sear
44.20.7280.2061
csear@proskauer.com

Stephen Severo
617.526.9640
ssevero@proskauer.com

PRIVATE EQUITY AND HEDGE FUND LITIGATION

Peter Duffy Doyle
212.969.3688
pdoyle@proskauer.com

Michael R. Hackett
617.526.9723
mhackett@proskauer.com

Timothy W. Mungovan
617.526.9412
tmungovan@proskauer.com

Kevin J. Perra
212.969.3454
kperra@proskauer.com

SEC ENFORCEMENT

Robert J. Cleary
212.969.3340
rjcleary@proskauer.com

Ralph C. Ferrara
202.416.5820
rferrara@proskauer.com

Joshua M. Newville
212.969.3336
jnewville@proskauer.com

Jonathan E. Richman
212.969.3448
jerichman@proskauer.com

Samuel J. Waldon
202.416.6858
swaldon@proskauer.com

BROKER-DEALER

Benjamin J. Catalano
212.969.3980
bcatalano@proskauer.com

Edward A. Kwalwasser
212.969.3515
ekwalwasser@proskauer.com

MARKETS AND TRADING/REGULATION

Edward A. Kwalwasser
212.969.3515
ekwalwasser@proskauer.com

Frank Zarb
202.416.5870
fzarb@proskauer.com

ERISA

Ira G. Bogner
212.969.3947
ibogner@proskauer.com

Adam W. Scoll
617.526.9486
ascoll@proskauer.com

EXECUTIVE COMPENSATION

Michael J. Album
212.969.3650
malbum@proskauer.com

Seth J. Safra
202.416.5840
ssafra@proskauer.com

EMPLOYMENT

Allan S. Bloom
212.969.3880
abloom@proskauer.com

Keisha-Ann G. Gray
212.969.3855
kgray@proskauer.com

WHISTLEBLOWER

Lloyd B. Chinn
212.969.3341
lchinn@proskauer.com

TRUSTS AND ESTATES

Henry J. Leibowitz
212.969.3602
hleibowitz@proskauer.com
David Pratt
561.995.4777
dpratt@proskauer.com

Jay D. Waxenberg
212.969.3606
jwaxenberg@proskauer.com

Stephanie E. Heilborn
212.969.3679
sheilborn@proskauer.com

BANKRUPTCY AND RESTRUCTURING

Martin J. Bienenstock
212.969.4530
mbienenstock@proskauer.com

Jeff J. Marwil
312.962.3540
jmarwil@proskauer.com

Vincent Indelicato
212.969.4248
vindelicato@proskauer.com

CYBERSECURITY/ INTELLECTUAL PROPERTY AND TECHNOLOGY

Daryn A. Grossman
212.969.3665
dgrossman@proskauer.com

Jeffrey D. Neuburger
212.969.3075
jneuburger@proskauer.com

Ryan P. Blaney
202.416.6815
rblaney@proskauer.com

PRIVATE CREDIT

Peter J. Antoszyk
617.526.9749
pantoszyk@proskauer.com

Stephen A. Boyko
617.526.9770
sboyko@proskauer.com

Gary J. Creem
617.526.9637
gcreem@proskauer.com

Steven M. Ellis
617.526.9660
sellis@proskauer.com

CAPITAL MARKETS

Peter Castellon
44.20.7280.2091
pcastellon@proskauer.com

Karen J. Garnett
202.416.6850
kgarnett@proskauer.com

Jeremy Leifer
852.3410.8048
jleifer@proskauer.com

Fabio A. Yamada
55.11.3045.1250
fyamada@proskauer.com

Daniel L. Forman
212.969.3096
dforman@proskauer.com

FCPA/OFAC/ANTI-MONEY LAUNDERING

Chantel L. Febus
212.969.3429
cfebus@proskauer.com

MERGERS & ACQUISITIONS

Lauren K. Boglivi
212.969.3082
lboglivi@proskauer.com

Will S. Chuchawat
310.284.4550
wchuchawat@proskauer.com

Steven Davis
44.20.7280.2049
sdavis@proskauer.com

Daniel Ganitsky
212.969.3186
dganitsky@proskauer.com

NON-COMPETE/TRADE SECRET DISPUTES

Steven M. Kayman
212.969.3430
skayman@proskauer.com

Proskauer