SECURITIES OPERATIONS

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REGULATORY UPDATE

September 1, 2019

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IN THIS ISSUE

Take Action Now

SEC Clarifies Investment Advisers' Proxy Voting Responsibilities and Application of Proxy Rules to Voting Advice

On August 21, 2019, the SEC published new guidance to assist investment advisers in fulfilling their proxy voting responsibilities. The guidance discusses, among other matters, the ability of investment advisers to establish a variety of different voting arrangements with their clients and matters they should consider when they use the services of a proxy advisory firm. In addition, the SEC issued an interpretation that proxy voting advice provided by proxy advisory firms generally constitutes a "solicitation" under the federal proxy rules and provided related guidance about the application of the proxy antifraud rule to proxy voting advice. Both of these actions explain the SEC's view of various non-exclusive methods entities can use to comply with existing laws or regulations, and how such laws and regulations apply.

Firms should take action now to:

- Review policies and procedures in light of the guidance in advance of next year's proxy season;
- Engage Legal, Compliance, and senior business personnel to assess the impact of any operational or other issues that arise from the review;
- Contact the SEC's Division of Investment Management staff with comments or questions.

SEC Announcement of New Proxy Voting Guidance and Interpretation:
https://www.sec.gov/news/press-release/2019-158

SEC Guidance on Firm Proxy Voting Responsibilities:
https://www.sec.gov/rules/interp/2019/ia-5325.pdf

SEC Interpretation and Guidance on Proxy Rule Applicability:
https://www.sec.gov/rules/interp/2019/34-86721.pdf

For more information, please contact info@mediantonline.com

SEC INVESTOR ADVISORY COMMITTEE TO HOLD TELEPHONE MEETING

On August 8, 2019, the SEC announced that its Investor Advisory Committee will meet telephonically on September 5, 2019 at 11:00 a.m. EDT to discuss and vote on a recommendation from its Investor as Owner Subcommittee regarding the proxy process. The public may dial in to the Investor Advisory Committee meeting by calling (800) 260-0719 in the United States or (651) 291-1170 outside the United States. The access code for the call will be 470756.

Agenda: https://www.sec.gov/spotlight/investor-advisory-committee-2012/iac090519-agenda.htm
Press Release: https://www.sec.gov/news/press-release/2019-147

SEC PROPOSES TO MODERNIZE REGULATION S-K DISCLOSURE REQUIREMENTS

On August 8, 2019, the SEC voted to propose rule amendments to modernize the description of business, legal proceedings, and risk factor disclosures that registrants are required to make pursuant to Regulation S-K. These disclosure items have not undergone significant revisions in over 30 years. The proposed amendments are intended to update the rules to account for developments since their adoption or last amendment, to improve these disclosures for investors, and to simplify compliance efforts for registrants. Specifically, the proposed amendments are intended to improve the readability of disclosure documents, as well as discourage repetition and disclosure of information that is not material. "The world economy and our markets have changed dramatically in the more than 30 years since the adoption of our rules for business disclosures by public companies. Today's proposal reflects these significant changes, as well as the reality that there will be changes in the future," said SEC Chairman Jay Clayton.

Comments Due: October 22, 2019
Notice Release: https://www.sec.gov/rules/proposed/2019/33-10668.pdf

SEC PUBLISHES FIRST FEE RATE ADVISORY FOR FISCAL YEAR 2020

On August 23, 2019, the SEC announced that in fiscal year 2020 the fees that public companies and other issuers pay to register their securities with the SEC will increase. The annual rate changes for fees paid under Section 6(b) of the Securities Act of 1933 and Sections 13(e) and 14(g) of the Securities Exchange Act of 1934 must take effect on the first day of each fiscal year. The Section 6(b) rate is also the rate used to calculate the fees payable with the Annual Notice of Securities Sold Pursuant to Rule 24f-2 under the Investment Company Act of 1940. The Section 6(b) fee rate applicable to the registration of securities, the Section 13(e) fee rate applicable to the repurchase of securities, and the Section 14(g) fee rates applicable to proxy solicitations and statements in corporate control transactions will increase to $129.80 per million dollars from $121.20 per million dollars.

Effective Date: October 1, 2019
Press Release: https://www.sec.gov/news/press-release/2019-160

SEC APPROVES FINRA PROPOSAL TO AMEND RULES GOVERNING RESEARCH REPORTS AND COMMUNICATIONS WITH THE PUBLIC

On August 16, 2019, the SEC approved a proposal by the Financial Industry Regulatory Authority ("FINRA") to amend FINRA Rules 2210 and 2241 to conform to the requirements of the Fair Access to Investment Research Act of 2017 ("FAIR Act"). FINRA Rule 2210 governs a FINRA member firm's advertising practices and other communications with the public, while FINRA Rule 2241 governs the publication of research reports concerning equity securities and the analysts that produce such research. The proposed rule changes would eliminate the "quiet period" restrictions in FINRA Rule 2241 on publishing a research report or making a public appearance concerning a covered investment fund and would create a filing exclusion under FINRA Rule 2210 for covered investment fund research reports.

Approval Order: https://www.sec.gov/rules/sro/finra/2019/34-86700.pdf

FINRA TO AMEND RULES 5130 AND 5131 REGARDING PUBLIC OFFERINGS

On August 2, 2019, the SEC published for comment a FINRA proposal to amend FINRA Rules 5130 and 5131. FINRA Rule 5130 is designed to protect the integrity of the public offering process by ensuring that FINRA members make bona fide public offerings of securities at the offering price and do not withhold or purchase securities in a public offering for their own benefit. FINRA Rule 5131 addresses abuses in the allocation and distribution of new issues. FINRA Rule 5131 specifically prohibits the practice of spinning, which is the allocation of new issues by a firm to executive officers and directors of the firm's current, former or prospective investment banking clients. The proposal would amend FINRA Rule 5130 and FINRA Rule 5131 to exempt additional persons from the scope of the rules, modify current exemptions to enhance regulatory consistency with the federal securities laws, address unintended operational impediments, and exempt certain types of offerings from the scope of the rules.

Notice Release: https://www.sec.gov/rules/sro/finra/2019/34-86558.pdf

FINRA ANNOUNCES NOMINATION PROCESS TO FILL UPCOMING FIRM VACANCIES ON THE NATIONAL ADJUDICATORY COUNCIL

On August 20, 2019, FINRA published notification of an upcoming election to fill one large firm and one mid-size firm seat on the National Adjudicatory Council ("NAC"), and announced the FINRA Nominating & Governance Committee ("NGC") nominees for these vacancies. Eligible individuals not nominated by the NGC who obtain the requisite number of valid petitions may be included as candidates on the ballot by following the petition procedures set forth in the notice and FINRA's by-laws. A formal notice will be mailed to the executive representatives of all eligible large and mid-size FINRA member firms on or about October 21, 2019.

FINRA Election Notice: https://www.finra.org/sites/default/files/2019-08/Election-Notice-082019.pdf

NASDAQ TO AMEND SCAR ROUTING STRATEGY CREDITS

On August 8, 2019, the SEC published for comment a proposal by The Nasdaq Stock Market LLC ("Nasdaq") to amend its SCAR credits at Equity 7, Section 118(a). The rule change revises the pricing for Nasdaq's recently adopted SCAR routing strategy in securities listed on all three tapes. SCAR is a routing option under which orders check the primary automated system for order execution and trade reporting owned and operated by Nasdaq for available shares, and simultaneously route to the other equity markets operated by Nasdaq, including the Nasdaq BX market ("Nasdaq BX"). The rule change adjusts Nasdaq's SCAR credits to align them with recent changes to the Nasdaq BX fee schedule. The rule, as amended, became operative on August 1, 2019.

Notice Release: https://www.sec.gov/rules/sro/nasdaq/2019/34-86609.pdf

NASDAQ TO AMEND CUTOFFS FOR ON-CLOSE ORDERS IN THE CLOSING CROSS

On August 13, 2019, the SEC published for comment a Nasdaq proposal to amend certain cutoff times for on-close orders entered for participation in the Nasdaq Closing Cross (the "Closing Cross") and to adopt a second reference price for limit-on-close orders. The Closing Cross is a price discovery facility that crosses orders at a single price and establishes the Nasdaq Official Closing Price ("NOCP") for a security. The Closing Cross was designed to create a robust close that allows for efficient price discovery through a transparent automated auction process. Nasdaq is proposing to preclude on-close orders from being cancelled or modified after 3:50 p.m. ET and to permit limit-on-close orders entered after 3:55 p.m. ET to be accepted and priced at or between certain reference prices. Nasdaq believes that the proposed changes will enhance price discovery, stability and transparency in the Closing Cross process.

Comments Due: September 9, 2019
Notice Release: https://www.sec.gov/rules/sro/nasdaq/2019/34-86642.pdf

NASDAQ TO MODIFY ITS CLOSING PRICE FOR EXCHANGE TRADED PRODUCTS

On August 19, 2019, the SEC published for comment a Nasdaq proposal to amend Rule 5754(b), which, in effect, would change how Nasdaq determines the NOCP for an exchange traded product ("ETP") if Nasdaq does not conduct a Closing Cross for the ETP. Thinly-traded ETPs are less likely to participate in the Closing Cross, which can result in a closing price that is based on the ETP's last sale price. Last sale prices of thinly-traded ETPs can be stale and not reflective of the value of the ETP. Therefore, Nasdaq proposes to utilize a time-weighted average based on the midpoint of the National Best Bid and National Best Offer prices. The proposed functionality of the Nasdaq proposal is similar to functionality of an NYSE Arca, Inc. proposal that has already been approved by the SEC and is operational.

Comments Due: September 13, 2019
Notice Release: https://www.sec.gov/rules/sro/nasdaq/2019/34-86705.pdf

NYSE TO AMEND ITS PRICE LIST RELATED TO CO-LOCATION SERVICES

On August 1, 2019, the SEC published for comment a proposal by the New York Stock Exchange LLC ("NYSE") to amend its price list related to co-location services and, specifically, its Partial Cabinet Solutions ("PCS") bundles. Currently, the NYSE has four PCS bundles, and each includes a partial cabinet, access to the Liquidity Center Network ("LCN"), internet protocol ("IP") network, the local area networks available in the data center, two fiber cross connections, and connectivity to a time feed. Two of the four PCS bundles include 10 Gigabit bandwidth, a lower bandwidth than other LCN connection options. The proposed change would lower the latency in the LCN connection for those two PCS bundles, which would improve the user connection at no additional cost as there are no proposed changes to the fees for the PCS bundles. NYSE expects to implement the change during the fourth quarter of 2019. It will announce the implementation date through a customer notice at a future date.

Notice Release: https://www.sec.gov/rules/sro/nyse/2019/34-86550.pdf

NYSE TO INCREASE MAXIMUM FINE FOR MINOR RULE VIOLATIONS

On August 16, 2019, the SEC published for comment a NYSE proposal to increase the maximum fine for minor rule violations from $2,500 to $5,000 in order to more closely align its minor rule plan with that of its affiliates. The NYSE has also proposed to add certain of its rules to the list of minor rule violations in Rule 9217, including rules governing authorized traders, crossing orders, registration and capital requirements of designated market makers, registration requirements, and supervision. The NYSE also proposes that all of the registration and other requirements set forth in Rule 345 be eligible for a minor rule fine.

Comments Due: September 12, 2019
Notice Release: https://www.sec.gov/rules/sro/nyse/2019/34-86696.pdf

NYSE AMERICAN TO AMEND ITS OPTIONS FEE SCHEDULE

On August 14, 2019, the SEC published for comment a proposal by the NYSE American LLC ("NYSE American") to amend its Options Fee Schedule to reduce the amount of Initiating Complex CUBE volume required for an American Trading Permit ("ATP") Holder to qualify for the Complex CUBE Cap Incentive ("Incentive") from 0.20% of Total Industry Customer equity and ETF option average daily volume ("TCADV") to 0.15% of TCADV. The proposed change is designed to incentivize ATP Holders to increase their options volume to qualify for the Incentive, which may, in turn, encourage firms to qualify for caps and incentives of their own, which ultimately should increase options volume directed to the NYSE American options market. The proposed fee modifications were implemented on August 9, 2019.

Comments Due: September 11, 2019
Notice Release: https://www.sec.gov/rules/sro/nyseamer/2019/34-86657.pdf

NYSE AMERICAN TO REDUCE MINIMUM ALLOWABLE PARAMETERS IN ITS RISK LIMITATION MECHANISM

On August 16, 2019, the SEC published for comment a NYSE American proposal to amend Rule 928NY to reduce the minimum allowable parameter for the transaction-based and volume-based settings in its risk limitation mechanism. The filing would align the minimum allowable parameter for the transaction-based and volume-based settings with the minimum allowable setting for the percentage-based setting, which the NYSE American reduced earlier this year. The proposed rule, as amended, would give the NYSE American the option to set uniform minimum exposure requirements, particularly for market makers who are obligated to utilize one of the three risk settings.

Comments Due: September 12, 2019
Notice Release: https://www.sec.gov/rules/sro/nyseamer/2019/34-86691.pdf

OCC RECEIVES AUTHORIZATION TO IMPLEMENT VANILLA OPTION MODEL AND SMOOTHING ALGORITHM

On August 20, 2019, the SEC published a notice of no objections to a proposal by the Options Clearing Corporation ("OCC") to modify its margin methodology regarding the estimation of prices for listed options contracts. The changes proposed are designed to resolve five limitations of both the OCC's current vanilla option model and its current smoothing algorithm, which should result in more accurate and consistent pricing methodologies. Previously, on June 28, 2019, the OCC filed with the SEC an advance notice filing of its proposal, which the SEC published for comment on July 31, 2019. The SEC received no comments on the proposal and, by not objecting to the proposal, authorized the OCC to implement its proposed changes as early as August 20, 2019.

Notice Release: https://www.sec.gov/rules/sro/occ-an/2019/34-86713.pdf

MSRB TO AMEND INTERPRETIVE NOTICE CONCERNING UNDERWRITERS OF MUNICIPAL SECURITIES

On August 5, 2019, the SEC published for comment a proposal by the Municipal Securities Rulemaking Board ("MSRB") to amend and restate its August 2, 2012 interpretive notice (the "2012 Notice") concerning the application of MSRB Rule G-17 to underwriters of municipal securities. MSRB Rule G-17 requires that municipal securities dealers and brokers deal fairly with all persons, including municipal entity issuers, and not engage in any deceptive, dishonest or unfair practice. The amendments in the proposed rule change are intended to update and streamline certain obligations specified in the 2012 Notice and, thereby, benefit issuers and underwriters alike by reducing the burdens associated with those obligations, including the obligation of underwriters to make written disclosures that itemize risks and conflicts that are unlikely to materialize during the course of a transaction, not unique to a given transaction or a particular underwriter where a syndicate is formed, and/or is otherwise duplicative.

Notice Release: https://www.sec.gov/rules/sro/msrb/2019/34-86572.pdf

Notable Enforcement Action

This month's enforcement actions mark a return to stiff penalties for supervisory and operational system failures, particularly those designed to detect violations of rules and regulations.

A firm was fined $250,000 and ordered to pay $512,261, plus interest, in restitution to customers for failing to establish and implement, as part of its anti-money laundering ("AML") compliance program, policies and procedures reasonably designed to detect and cause the reporting of suspicious activity in its primary business—accepting and liquidating customers' deposits of microcap securities. As a result, the firm failed to detect or investigate numerous warning signs of suspicious activity. The firm's customers deposited certificates representing billions of shares of companies with little or no established business, including companies that had recently undergone reverse mergers that dramatically changed their business strategy. The firm's customers routinely liquidated those shares within days after depositing them, and then quickly withdrew the proceeds. Some of those customers had been disciplined by regulatory authorities, had personal or professional ties to the companies whose stock they were liquidating, or otherwise had questionable backgrounds, and virtually all of the activity involved penny stocks. In addition to the fine and customer restitution, the firm was suspended from accepting deposits of stock certificates and liquidating previously deposited certificated securities until it implements measures to remedy its AML system deficiencies. The findings also state that the firm, acting through its manager of operations, affixed its CEO's signature to representations required by its clearing firm, thereby representing that the CEO had reviewed customers' stock deposits, even though she had not actually done so. The firm also charged more than five percent of the principal amount on stock transactions, totaling $512,261, on more than 5,500 occasions, representing more than 60% of the firm's overall trading volume during the period. In doing so, the firm failed to enforce its written supervisory procedures ("WSPs") governing charges for transactions.
(**FINRA Case #2016051209102**)
https://www.finra.org/sites/default/files/fda_documents/2016051209102%20Spencer%20Edwards%2C%20Inc.%20SEI%20CRD%2022067%20AWC%20jm%20%282019-1563547760964%29.pdf

A firm was censured and fined $225,000 for failing to report or inaccurately reporting over-the-counter ("OTC") options positions to the Large Options Position Reporting system ("LOPR"), and untimely reported options positions to the FINRA Trade Reporting Facility. The firm also failed to establish and maintain a supervisory system and WSPs reasonably designed to achieve compliance with FINRA rules related to the reporting of options positions to the LOPR.
(**FINRA Case #2013038502101**)
https://www.finra.org/sites/default/files/fda_documents/2013038502101%20Nomura%20Securities%20International%2C%20Inc.%20CRD%204297%20AWC%20jm%20%282019-1563545959681%29.pdf

A firm was censured, fined $225,000 and ordered to pay $152,488.59, plus interest, in restitution to customers for failing to identify and apply sales charge discounts to certain eligible purchases of unit investment trusts ("UITs"). As a result, customers paid excessive sales charges of $152,488.59. The firm also failed to supervise purchases and sales of UITs in two respects. First, the firm failed to establish, maintain and enforce a supervisory system and WSPs reasonably designed to achieve compliance with applicable securities laws, regulations and FINRA rules regarding the crediting of all available sales charge discounts to customers' eligible UIT purchases. Among other things, the firm had no WSPs that discussed the application of rollover discounts and no surveillance tools to identify available rollover discounts. Second, the firm failed to establish, maintain and enforce a supervisory system and WSPs reasonably designed to supervise UIT trading. The firm's surveillance alert system failed to detect switching of UITs and other products, and inadvertently excluded UITs from consideration, which the firm failed to discover for years.
(**FINRA Case #2016050947701**)
https://www.finra.org/sites/default/files/fda_documents/2016050947701%20Citigroup%20Global%20Markets%20Inc.%20CRD%207059%20AWC%20sl%20%282019-1563668376197%29.pdf

A firm was censured, fined $55,000 and required to revise its WSPs for failing to establish, maintain and enforce written policies and procedures that were reasonably designed to prevent trade-throughs of protected quotations in National Market System ("NMS") stocks when it executed these orders internally but failed to simultaneously send intermarket sweep orders ("ISOs") to one or more markets displaying protected quotations in that stock. The firm executed orders internally by trading as principal or crossing the order as agent, thus acting as a trading center, but failed to simultaneously send ISOs to one or more markets displaying better-priced quotations resulting in in trade-throughs. The firm sent ISOs to other trading centers without routing additional limit orders to one or more other trading centers displaying better-priced protected quotations.
(**FINRA Case #2015045281603**)
https://www.finra.org/sites/default/files/fda_documents/2015045281603%20Sanford%20C.%20Bernstein%20%26%20Co.%2C%20LLC%20CRD%20104474%20AWC%20va%20%282019-1564186775129%29.pdf

A firm was censured and fined $75,000 for failing to accurately calculate its net capital resulting in net capital deficiencies in amounts ranging from $3,348 to $449,666. The firm improperly calculated its customer reserve formula on one occasion and, as a result, failed to make a sufficient deposit in its reserve account, resulting in a hindsight deficiency of $59,590. As a result of the firm's failure to properly calculate its net capital and customer reserve requirements, it created and maintained inaccurate books and records. The firm's failure to accurately calculate its net capital also caused it to file Financial and Operational Combined Uniform Single ("FOCUS") reports that inaccurately reported its net capital. Consequently, the firm failed to establish, maintain and enforce a supervisory system, including WSPs, reasonably designed to ensure its compliance with net capital and customer reserve requirements. The firm also failed to timely and properly close out open failure to deliver positions. The firm routed and/or executed short sales in these securities without first borrowing or arranging to borrow the security.
(**FINRA Case #2016052177801**)
https://www.finra.org/sites/default/files/fda_documents/2016052177801%20Lime%20Brokerage%2C%20LLC%20CRD%20104369%20AWC%20jm%20%282019-1563545959499%29.pdf

A firm was censured and fined $200,000 for failing to disclose material facts while assisting with the preparation and circulation of a confidential information memorandum ("CIM") to accredited investors for a private placement of notes. The issuer was supposed to provide the proceeds of the notes to a film production company for the advance funding of anticipated state tax credits. The CIM disclosed that in addition to a two percent commission, the firm would earn a certain percentage of profits on the sale of tax credits, but failed to disclose that the firm would earn half of the profits on the sale. The CIM also failed to disclose that one of the firm's registered representatives was vice president of the issuer. The firm also omitted material facts from a private placement memorandum ("PPM") for municipal bonds underwritten by the firm to finance the construction of a community recreation center. Although the firm verbally disclosed the loan agreement to investors, it failed to disclose in the PPM that the issuer had threatened to default on an earlier series of bonds and bond anticipation notes and that a loan agreement existed between the issuer and firm. The firm failed to disclose information about the finances of both the issuer and firm. The firm also failed to establish, document and maintain a written system of risk management controls and supervisory procedures relating to the firm's provision of direct market access to its traders. The firm failed to establish risk management controls and supervisory procedures to limit its financial exposure resulting from permitting its traders to access alternative trading systems sites, such as establishing an aggregate trading limit for daily buys and sells. FINRA found that in the firm's annual chief executive officer certification, it failed to certify that its risk management controls and procedures complied with the provisions of SEC Rule 15c3-5.
(**FINRA Case #2017052424001**)
https://www.finra.org/sites/default/files/fda_documents/2017052424001%20Ross%20Sinclaire%20%26%20Associates%2C%20LLC%20CRD%2025440%20AWC%20jm%20%282019-1563549559244%29.pdf

A firm was censured and fined $150,000 for publishing seven research reports about an issuer without disclosing that its research analyst who authored the reports was engaged in employment discussions with the issuer that constituted an actual, material conflict of interest. The research analyst's candidacy for employment at the issuer was clearly viable, and the issuer and the research analyst had expressed mutual interest and taken concrete steps in furtherance of their employment discussions. The firm's failure to disclose the actual, material conflict of interest arising from the research analyst's employment discussions with the issuer in the research reports authored by him and published by the firm made those reports misleading.
(**FINRA Case #2017052842901**)
https://www.finra.org/sites/default/files/fda_documents/2017052842901%20Robert%20W.%20Baird%20CRD%208158%20AWC%20va%20%282019-1563547760840%29.pdf