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## 1940 Act Issues to Consider During the Pandemic

In light of the outbreak of coronavirus disease 2019 (COVID-19) and operational disruptions throughout the world, below is a short list of issues that registered investment companies and fund managers should consider at the current time.

- **In-person board meetings:** On March 13, the SEC issued an order under the Investment Company Act of 1940 (“1940 Act Order”), allowing fund boards to meet telephonically or by video conference to consider and vote on matters that would otherwise require an in-person vote.<sup>1</sup> The relief applies whenever reliance upon it is necessary or appropriate due to circumstances related to current or potential effects of COVID-19 and is available until June 15, 2020. The SEC’s Division of Investment Management previously provided no-action relief for the period from March 4 to June 15.<sup>2</sup>
- **SEC filings:** The 1940 Act Order also provides relief from the timeliness requirements of Form N-CEN, Form N-PORT, and Form N-23C-2, when a fund is unable to meet a deadline due to circumstances related to current or potential effects of COVID-19. The relief for Forms N-CEN and N-PORT applies to filing obligations for which the original due date is on or after March 13 but on or prior to April 30, 2020, while the relief for Form N-23C-2 extends to June 15, 2020. A separate order under the Investment Advisers Act of 1940 provides timeliness relief for Form ADV and Form PF filings and for Form ADV Part 2 client delivery obligations, when the original due date is on or after March 13 but on or prior to April 30, 2020.<sup>3</sup> The SEC previously provided relief from timeliness requirements for certain filings under the Securities Exchange Act of 1934.<sup>4</sup> Note that filings not covered by the orders continue to be required on a timely basis, including filings on Form N-LIQUID, Form N-CR, and Form N-MFP, although it is possible that the SEC will consider issues with these forms on an individualized basis. The SEC provided information on contacting the staff with issues, including issues with these filings, in a press release announcing the actions.<sup>5</sup>
- **Delivery of prospectuses and shareholder reports:** The 1940 Act Order also provides relief from the obligations to timely transmit annual and semiannual reports to shareholders and to file them with the SEC. The relief applies when the original due date is on or after March 13 but on or prior to April 30, 2020, and the fund is unable to prepare or transmit the report due to circumstances related to current or potential effects of COVID-19. In addition, the SEC announced that it would not provide a basis for an SEC enforcement action if a fund does not timely deliver a current prospectus because of circumstances related to COVID-19, when delivery was originally required during this period. The position is not available to an initial purchase by the investor of the fund’s shares.

- **Business continuity plans:** Business continuity at the current time is key. In most cases, those plans already are in effect. Consideration should be given to contingency planning in the event that fund managers, transfer agents, pricing services, or other service providers are unable to provide services because of employee absences. Funds and fund managers should make and communicate revisions to their plans as they adjust to the developing environment.
- **Liquidity risk management:** Fund holdings might become illiquid or less liquid should markets close or freeze up, or if market depth in some securities or asset classes is significantly reduced. Under these circumstances, liquidity risk management program administrators should be prepared to reclassify the liquidity classifications for some classes of investments and to take any other actions necessary to manage liquidity under their liquidity risk management programs. If a fund's illiquid assets exceed 15% of its net assets, or if its highly liquid investments fall below its highly liquid investment minimum ("HLIM") for more than seven consecutive calendar days, the fund will be required to promptly report to the fund's board and to the SEC on Form N-LIQUID. Program administrators should have these communication protocols prepared. In addition, for those funds that currently hold primarily highly liquid assets, and therefore are not required to have an HLIM, the administrator should examine whether the fund can still qualify for that status.
- **Valuation:** Funds should examine whether they are able to obtain valid prices for their investments, especially in markets that may be closed or have limited availability. Experience from the 2008 financial crisis shows that vendor reassurances as to the quality of their pricing information may provide false comfort,

so vendor prices should be checked for reliability. At this time, we do not expect the SEC to provide relief from the daily pricing requirement.

- **Redemptions:** Under Section 22(e) of the 1940 Act, open-end funds generally may not suspend the right of redemption unless the New York Stock Exchange is closed, or the SEC provides guidance that daily redemptions are not required because trading is restricted or an emergency exists. At this point, funds should assume that they must continue to provide daily redemptions. Funds should review any borrowing arrangements that may need to be utilized. We are closely monitoring for any relevant guidance from the SEC or its staff on this topic.
- **Cybersecurity:** Firms are at increased risk of cyberattacks, particularly with the use of remote offices and telework. Anxious employees may be more vulnerable to email phishing attacks. Employees should be reminded of the continued need for vigilance.
- **Prospectus disclosures:** Funds should review their prospectus disclosures, and particularly their risk disclosures. It may be appropriate to add a pandemic risk factor if this risk is not already addressed. However, funds have different risk profiles, and there is no one-size-fits-all solution for the necessary disclosures.
- **Annual meetings:** The SEC staff has provided guidance to both operating companies and funds that is intended to provide regulatory flexibility to companies seeking to change the date and location of the meetings and use new technologies, such as "virtual" shareholder meetings that avoid the need for in-person shareholder attendance, while at the same time ensuring that shareholders and other market participants are informed



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Please do not hesitate to reach out to your Stradley Ronon contact, or to any member of Stradley's Coronavirus Task Force, with any questions and concerns you may have during this period.

of any changes.<sup>6</sup> The guidance notes that the ability to conduct a “virtual” meeting is governed by state law, where permitted, and the issuer’s governing documents.

- **Exchange-traded funds:** ETFs should consider many of the issues outlined above, including the ETF-specific provisions in the liquidity risk management rule, as well as the potential widening of premiums or discounts.
- **Money market funds:** Money market funds may face their own liquidity and valuation challenges and reporting requirements, which will vary depending on the type of money market fund at issue.

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<sup>1</sup> Release No. IC-33817 (Mar. 13, 2020), <https://www.sec.gov/rules/other/2020/ic-33817.pdf>. The various forms of relief provided by the SEC are subject to conditions that are set out in the respective orders, such as subsequent ratification of votes, notice to the SEC of filing delays, and website disclosure of issues with the delivery of shareholder reports, prospectuses, and Form ADV client brochures.

<sup>2</sup> SEC Division of Investment Management, Staff Statement on Fund Board Meetings and Unforeseen or Emergency Circumstances Related to Coronavirus Disease 2019 (COVID-19) (Mar. 4, 2020), <https://www.sec.gov/investment/staff-statement-im-covid-19>.

<sup>3</sup> Release No. IA-5463 (Mar. 13, 2020), <https://www.sec.gov/rules/other/2020/ia-5463.pdf>.

<sup>4</sup> Release No. 34-88318 (Mar. 4, 2020), <https://www.sec.gov/rules/other/2020/34-88318.pdf>.

<sup>5</sup> Press Release 2020-63, SEC Takes Targeted Action to Assist Funds and Advisers, Permits Virtual Board Meetings and Provides Conditional Relief from Certain Filing Procedures (Mar. 13, 2020), <https://www.sec.gov/news/press-release/2020-63>.

<sup>6</sup> Staff Guidance for Conducting Annual Meetings in Light of COVID-19 Concerns (Mar. 13, 2020), <https://www.sec.gov/ocr/staff-guidance-conducting-annual-meetings-light-covid-19-concerns>.

## ABOUT STRADLEY RONON

This pandemic is unprecedented. To continue to assist our clients and friends, we have implemented contingency plans designed to maintain operations and to ensure that we can continue to provide the highest level of service during this rapidly changing environment, while also protecting the health of our personnel. We will continue to review, update, and adapt those plans as the situation progresses, and will certainly keep you apprised of any developments that might impact your business.