



Date May 14, 2020

Updated SEC Guidance for Investment Advisers

Audit Provision/Custody Rule

On April 27, 2020, the Division of Investment Management of the Securities and Exchange Commission (“SEC”) updated Staff Responses to Questions About the Custody Rule. Among other things, the updated Responses provide that, in light of the COVID-19 pandemic, the Staff would not recommend enforcement action for a violation of the Custody Rule (Rule 206(4)-2 of the Investment Advisers Act of 1940) against an investment adviser to a pooled investment vehicle where the adviser (i) is relying on the “audit provision” of the Rule to avoid a surprise audit and (ii) reasonably believed the pooled investment vehicle’s audited financial statements would be distributed within 120-days after the end of its fiscal year, but failed to have them distributed within the foregoing deadlines under “certain unforeseeable circumstances.”¹ While not stated explicitly, “certain unforeseeable circumstances” relates to circumstances of the COVID-19 pandemic. Note, that the 120-day period is 180-days in the case of a fund of funds and 260-days in the case of a “top tier” pooled investment vehicle.

PPP Disclosure to Clients

On April 27, 2020, the SEC updated the Division of Investment Management Coronavirus (COVID-19) Response FAQs. Among other things, the updated Response FAQs provide that an investment adviser that receives a Paycheck Protection Program (PPP) loan or other type of financial assistance would be required to disclose that fact to clients, including the “nature, amounts and effects of such assistance,” if the circumstances leading the adviser to seek the PPP loan or the financial assistance constitute material facts relating to the adviser’s relationship with its clients. The SEC guidance gave the following examples of when such disclosure should be made: if the adviser (i) requires financial assistance to pay salaries of its employees who are primarily responsible for performing advisory functions for clients; or (ii) is experiencing conditions that are reasonably likely to impair its ability to meet contractual commitments to its clients.² An investment adviser is a fiduciary, and consistent with its fiduciary duty, the adviser is

¹ Question VI.9 available at https://www.sec.gov/divisions/investment/custody_faq_030510.htm

² Question II.4. available at <https://www.sec.gov/investment/covid-19-response-faq>

required to make “full and fair disclosure” to clients of all material facts relating to the advisory relationship. Since an applicant for a PPP loan must certify that “current economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant,” it is unlikely that the SEC would not deem acceptance of a PPP loan as relevant to the financial condition of the adviser, and therefore, a material fact that would require disclosure in an investment adviser’s Form ADV.

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If you have questions about how the SEC’s guidance on COVID-19 related matters affects your business, please contact Meryl Wiener, any of the undersigned or your regular Warshaw Burstein attorney.

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