

SEC Proposes Rule Requiring Investment Advisers to Adopt Business Continuity and Transition Plans

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The Securities and Exchange Commission (“SEC”) has recently proposed a new rule that would require SEC-registered investment advisers to adopt and implement written business continuity and transition plans (“BCP”) reasonably designed to address operational and other risks related to a significant disruption in the investment adviser’s operations. The proposed rule would amend current Rule 204-2 under the Investment Advisers Act of 1940 (the “Advisers Act”) and require certain recordkeeping of such plans. The proposed rules are open to public comment until September 6, 2016.

In Release No. IA-4439, the SEC underscores that investment advisers owe a fiduciary duty of care to their clients and are obligated to take steps to protect client interests from being placed at risk as a result of the adviser’s inability to provide advisory services. Specifically, these risks may include instances of natural disasters, acts of terrorism, cyber-attacks, equipment or system failures, the adviser is unable to access its physical location and/or facilities, or the unexpected loss of a service provider, facilities, or key personnel. The SEC warns that failure to evaluate and adopt a plan addressing these risks could go so far as to amount to fraud and deceit, as an adviser should not hold itself out as providing advisory services if it is unable to protect its clients’ interests in the event these situations occur.

If adopted, new Rule 206(4)-4 under the Advisers Act would prohibit SEC-registered investment advisers from providing investment advice “unless the adviser adopts and implements a written business continuity plan and reviews that plan at least annually.” The amended Rule 204-2 would require advisers to keep such plans for at least five years. These BCPs must be “reasonably designed to address the operational and other risks of an adviser and ...need only take in account the risks associated with its particular operations, including the nature and complexity of the adviser’s business, its clients, and its key personnel” and specifically must address both continuity after a business disruption and in the event the adviser is unable to continue providing advisory services. As proposed, the plans should include policies and procedures that address each of the following:

- Maintenance of critical operations and systems, and the protection, backup, and recovery of data in the event of a significant business disruption;
- Pre-arranged alternate physical location(s) of the adviser’s office(s) and/or employees;
- Communications with clients, employees, service providers, and regulators, which may entail developing and implementing training programs and maintaining database(s) of the contact information of key personnel and clients;
- Identification and assessment of third-party services critical to the adviser (including evaluating those parties’ BCPs), which the SEC believes should include those providing services related to portfolio management, custody of client assets, trade execution and related processing, pricing, client servicing and/or recordkeeping, and financial and regulatory reporting; and
- Plan of transition that accounts for a possible winding down of the adviser’s business or the transition of its business to others in the event it is unable to continue providing advisory services, which, among other things, should (i) account for transitions in both normal and stressed market conditions, (ii) contain policies and procedures intended to safeguard, transfer and/or distribute client assets during transition, (iii) contain information regarding the corporate governance structure of the adviser, (iii) address any special instructions given by specific clients, (iv) identify material financial resources available to the adviser, and (v) include an assessment of applicable law and contractual obligations governing the relationship between the adviser and its client.

Foley Hoag LLP will continue to monitor the progress of the proposed rule and provide updates to its clients. The full text of the proposed

rule is [available here](#).

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