

[Securities Regulation Daily Wrap Up, INVESTMENT ADVISERS—SEC issues FAQ on self-reporting initiative for undisclosed mutual fund fee conflicts, \(May 2, 2018\)](#)

Securities Regulation Daily Wrap Up

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The SEC's Division of Enforcement has issued a document answering frequently asked questions ("FAQ") regarding its Share Class Selection Disclosure ("SCSD") Initiative, which encourages advisory firms to self-report undisclosed conflicts of interests regarding mutual fund advisory fees and to return excessive fees to investors in exchange for favorable settlement terms.

[According to](#) Enforcement Asset Management Unit Co-Chief Dabney O'Riordan, "It appears that many investment advisors are working diligently to evaluate whether they can take advantage of the initiative and we believe that providing these FAQs will help them make that determination."

SCSD Initiative. The SEC [launched](#) the SCSD Initiative in February 2018. Under the Initiative, investment advisers that failed to make required disclosures relating to the selection of mutual fund share classes that paid the adviser (as a dually registered broker-dealer) or its related entities or individuals an Investment Company Rule 12b-1 fee when a lower-cost share class for the same fund was available to clients can receive favorable settlement terms by self-reporting these disclosure failures, including a Division recommendation that the adviser should not have to pay a civil monetary penalty.

When the SEC [announced](#) the SCSD Initiative, it pointed to a number of enforcement actions the Enforcement Division has brought against advisory firms for failing to disclose these conflicts of interests while recommending higher-fee share classes, including actions against [SunTrust Investment Services](#), [Envoy Advisory](#), [Cadaret, Grant & Co.](#), and [Manarin Investment Counsel](#). More recently, the SEC [charged](#) three firms for failing to disclose lower-fee share classes, resulting in the reimbursement to investors of \$12 million to settle the SEC's charges. At the SEC's recent compliance conference, O'Riordan brought attention to the SCSD Initiative and [warned](#) that the deadline for self-reporting disclosure violations is June 12, 2018, after which the Division might not offer such favorable settlement terms.

Frequently asked questions. In response to one frequently asked question, the Division [states](#) that it does not plan to offer fundamentally different settlement terms based on the severity and scope of the conduct. It also clarifies that self-reporting must be made in the manner detailed in the announcement, which instructs a specific email address and a physical address relating to the SCSD Initiative. Reporting to the Office of Compliance Inspections and Examinations (OCIE) would not suffice.

The FAQ also advises that even if OCIE has already conducted an exam regarding these issues, an adviser can still self-report under the Initiative. Interactions with OCIE staff will not constitute self-reporting under the Initiative, the Division explains. The Division recommends that firms contacted by Enforcement staff regarding the conduct described in the SCSD announcement before the Initiative was announced contact the Enforcement attorney working on that case to determine that firm's eligibility.

The FAQ specifies that the Initiative applies to entities acting as an investment adviser in recommending, purchasing, or holding 12b-1 paying share classes when a lower-cost share in the same fund was available. It also makes clear that an adviser must disclose both conflicts associated with making investment decisions in light of the receipt of 12b-1 fees as well as selecting the more expensive 12b-1 fee, and that an adviser is eligible for the SCSD Initiative if it failed to disclose either or both of those conflicts.

The FAQ notes that, in response to a question about whether investments in money market funds would qualify for the Initiative, any investment adviser meeting the definition of "self-reporting adviser" in the announcement is eligible to participate in the Initiative and that it does not differentiate between types of funds.

In addition, the FAQ provides a non-exhaustive list of examples about what it means for a lower-cost share to be "available" for the same fund. The FAQ advises that firms should consult with counsel regarding potential collateral consequences stemming from a settlement under the initiative, noting that settlement terms under the Initiative will require certain undertakings.

As stated, the deadline for self-reporting under the SCSD Initiative is June 12, 2018, and the Commission does not anticipate extending that deadline, according to the FAQ.

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