MAYER | BROWN

14TH ANNUAL

Investment Management Regulatory University

WEBINAR SERIES

September 9, 2020

Stephanie Monaco
(202) 263-3379
SMonaco@mayerbrown.com

Leslie Cruz
(202) 263-3337
LCruz@mayerbrown.com

Chris Chapman
+44 20 3130 3344
CChapman@mayerbrown.com

Oliver Yaros
+44 20 3130 3698
OYaros@mayerbrown.com

J. Paul Forrester
(312) 701-7366
JForrester@mayerbrown.com

Jeffrey Taft
(202) 263-3293
JTaft@mayerbrown.com

GDPR: What Current and Prospective SEC-Registered Investment Advisers Need to Know

EU & UK laws: What is the GDPR?

- The General Data Protection Regulation (GDPR) is EU legislation that is directly effective in all member states and throughout the European Economic Area and in the UK. Entities outside of Europe (including in the US) may be subject to the GDPR if the organization is targeting or collecting data related to people in the EU.

- The GDPR regulates how businesses deal with personal data and confers rights on individuals - broadly, to know who has their personal data, what it is being used for and (sometimes) to object to its use or require its deletion.

- Breaches of the GDPR are enforced by local regulators – these regulators have the power to levy large fines of €20 million or 4% of global turnover, whichever is higher.

- The GDPR takes precedence over any conflicting legislation in the EU member states. However, member states can adopt supplementary laws in certain defined areas, including in the financial services industry, *e.g.* anti-money laundering frameworks, etc.

GDPR – Key issues to be addressed

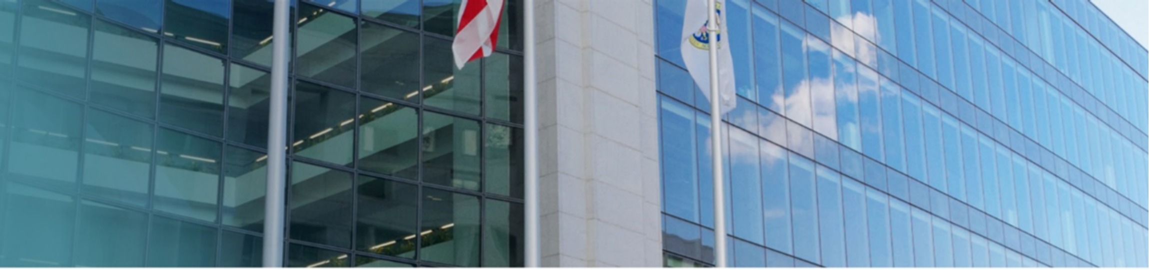
- Identifying the entities that must comply (controllers and processors)
- Identifying the scope of data and activities covered: "Processing" data includes uploading data to an internal/external platform, reading, reviewing, printing, redacting, disclosing, transferring/sending by email
- Ensuring compliance with the data protection principles: In particular fairness / transparency, purpose limitation and data minimisation
  - Notices to employees or others can be adapted to include data privacy information
- Identifying a legal basis for processing relevant to litigation (Article 6(1)):
  - Data subject consents (must be "freely given")
  - Necessary for compliance with a legal obligation to which the controller is subject
  - Necessary for the purposes of the legitimate interests pursued by the controller or by a third party, subject to interests of the data subject
- Identifying a basis to transfer the personal data from Europe to the US

Basis for Data Transfer Outside Europe (1)

- Adequacy decision (the US does not offer “adequate protection” under the GDPR standards)
- Data subject gives “explicit” consent
- US-EU Privacy Shield (but now invalidated)
- Intra-group transfers within a group of companies with approved Binding Corporate Rules
- Standard Contractual Clauses (aka Model Clauses) (NB non-negotiable)
  - Onward transfer from the data importer to a third party
  - Many legal matters will require the transfer of data to multiple parties, *e.g.* to lawyers and eDiscovery technology providers, etc., for review and analysis, so multiple agreements may be needed.

Basis for Data Transfer Outside the EEA (2)

- Article 49 derogation: the transfer is “necessary for the establishment, exercise or defence of legal claims”
  - What does “necessary” mean?
  - Open question as to how these exceptions will be interpreted in the context of US discovery
- Article 48: a foreign court order to transfer or disclose personal data does not make those actions automatically legal in the EU:
  - *Any judgment of a court or tribunal and any decision of an administrative authority of a third country requiring a controller or processor to transfer or disclose personal data may only be recognised or enforceable in any manner if based on an international agreement, such as a mutual legal assistance treaty, in force between the requesting third country and the Union or a Member State, without prejudice to other grounds for transfer pursuant to this Chapter.*
- Ways to comply:
  - Mutual Legal Assistance Treaty (MLAT)
  - Local regulator issues a compulsory document production notice to assist US enforcement authority
  - Hague Convention – assistance of local courts – BUT subject to restrictions in various jurisdictions



Discussion points

- Assurances as a condition of registration with the SEC as an investment adviser
- Practical issues:
  - Consent
  - Data types
  - Legal compulsion
  - Other gateways
- Conclusion and practical tips

US Privacy and Cybersecurity

SEC Focus on Cybersecurity

- OCIE - 2020 Examination Priorities (Jan. 7, 2020)
  - Protection of clients’ personal financial information
  - Areas of focus include the following: governance and risk management, access rights and controls, data loss prevention, vendor management, training and incident response and resiliency
- OCIE - Cybersecurity and Resiliency Observations (Jan. 27, 2020)
  - Concerns within areas of focus
  - Key takeaways from the observations

Privacy and Cyber Risks in WFH Environment

- Increased risks presented
  - Fewer controls over employees and work environment
  - Client data potentially less secure for variety of reasons
- OCIE's COVID risk alert
  - Protection of investor information
  - Business continuity (IA and its service providers)
- Current client issues in privacy and cyber area
  - Cyber-attacks/ransomware, phishing emails and service provider issues

Evolving US Privacy Landscape

- US has sector-specific federal legislation (financial services, health care, and education) and marketing restrictions.
- Title V of the Gramm-Leach-Bliley Act is the primary federal privacy law for financial information and implemented through regulations issued by the SEC, FTC, federal banking agencies and state insurance regulators.
- Congress has considered and debated enhanced federal privacy laws but nothing likely to be enacted in 2020.
- Next Congress is expected to pick-up this issue in 2021.

Evolving US Privacy Landscape

- The California Consumer Privacy Act (CCPA) effectively sets a floor for national data privacy standards, as it will be burdensome for organizations to create two separate frameworks for data privacy.
- The CCPA went into effect on January 1, 2020, with enforcement beginning on July 1, 2020.
- After the CCPA was passed, other states began to draft and enact similar data privacy regulations.
- New privacy initiative, California Privacy Rights & Enforcement Act (CPRA), will be on the November 2020 ballot and would ultimately replace the CCPA.

Key Takeaways for Financial Services Firms

- Revisit cybersecurity policies, procedures and implementation in this WFH environment.
- Manage risks of WFH environment with additional controls and training.
- Review third party vendor risk management onboarding and oversight procedures.
- Develop a scalable approach for addressing new state privacy and cyber requirements.

ESG (Re)volution: How to Get Your Share of the $30 trillion (and Rapidly Rising) of AUM in an Evolving Regulatory Landscape

ESG – Mayer Brown

- Our ESG group webpage
- Our ESG Perspectives
- Our ESG Events
- Our ESG Snapshots
- Our own ESG Commitment

ESG - You

- ESG AUM is currently around $30 trillion
- While initially an exclusionary “screen” for equity investments, ESG is now increasingly employed across most asset classes and is moving to exclusion to integration as part of the investment decision-making process
- ESG funds are popular and ESG fund-raising and re-branding is accelerating
- BUT:
  - No standard ESG definition and ESG “taxonomies” are evolving (and will continue to do so)
  - No standardized data
  - No standard use/application of data

MAYER | BROWN

Green Finance Rising

- Global green finance now around $400 billion and growing rapidly
- Since COVID-19, social and sustainable issuance has taken off
- Continuing refinement/improvement of related “principles” to mitigate “greenwashing” (most recently in June 2020)
- “Greenium” (i.e., the premium for a security being green) remains elusive; but issuers seem not to care
- Differences in use of proceeds (possibly material) continue to exist

And…the SEC Wants to Know About Your ESG

- Last January, the SEC's OCIE announced that ESG is a focus area and an examination priority for 2020
  - See our related Legal Update
- This follows several years' of ESG interest in SEC examinations, and is focused on the following:
  - What kind of scoring and benchmarks are being used, particularly whether the firm uses a third-party system or a proprietary one, and applicable written procedures.
  - Lists of particular ESG investments made or recommended, and the ESG scoring for each.
  - Internal processes and policies, including compliance evaluations or internal audits related to ESG investments and information on applicable service providers.
  - Returns on ESG investments (*e.g.*, most and least profitable investments, as well as financial performance metrics and non-financial ESG performance metrics).
  - All marketing materials that describe the ESG program to current or prospective investors.

And…the DOL Wants to Restrict ERISA Funds

- On April 23, 2018, the U.S. Department of Labor (“DOL”) issued new guidance under the Employee Retirement Income Security Act of 1974, as amended (“ERISA”) on the extent to which a plan fiduciary can consider ESG factors when making investment decisions and the use of plan assets in exercising shareholder rights
  - See our related Legal Update
- Industry (including heavyweights like BlackRock and Fidelity) is fighting back

So, What Does That Mean…

- Risks to asset managers:
  - Misrepresentation/reputation
  - Increased Regulatory Scrutiny/Activity
    - SECs RFC for Names Rule (see our related Legal Update)
    - SEC Conflicted about Mandatory Disclosure (although human capital was included – sort of – in the most recent revision to Regulation S-K disclosure; several comment letters had suggested that climate change be addressed; others strongly opposed such "policy-making" rules)
    - EU Moving More Quickly (EU Green Deal; EU Taxonomy), but the EU requirements may not "travel" well and, in any event, may not reflect an asset manager's judgments about relevant criteria and scoring

MAYER | BROWN

LIBOR: Is Going Away and It (Probably) Won’t Be Pretty

LIBOR Transition – Mayer Brown

- Our IBOR Transition portal
- Our IBOR Transition Task Force
- Our IBOR Transition Digest
- Our IBOR Transition Webinars
- Our Eye on IBOR Transition blog

LIBOR - Primer

- The London Interbank Offered Rate (LIBOR) was developed to provide an objective proxy for bank funding costs following prime rate scandals in the 1980s
- Despite its humble origins, LIBOR is the benchmark rate for over $300 trillion of swaps, securities, loans, mortgages and consumer products
- About 90% of global LIBOR exposure is interest rate swaps
- However, there are around $30 trillion of affected cash products (i.e., bonds, loans, mortgages, etc.)
- Following bank capital reforms in the early 2000s, interbank term borrowing fell to dangerously low levels and subsequently led to manipulation, since more LIBOR quotes were estimates rather that based on actual transactions

The Global Efforts to Find Alternative Benchmarks

- In response, global financial regulators decided that LIBOR had become an inappropriate benchmark and launched a global effort to replace LIBOR initiated by the UK's Financial Conduct Authority announcing in 2017 that it would not compel LIBOR panel banks to provide LIBOR quotes after December 31, 2021
- Most affected jurisdictions turned to liquid transparent overnight markets for "risk-free rates" (RFRs)
- However, most RFRs need "adjustments" to be made "comparable" to LIBOR
- This has proven more difficult and time-consuming than many anticipated

LIBOR Transition

- "Comparability" is a low bar; much higher is the required determination that an adjusted RFR is "fit for purpose"
  - See our related Legal Update and subsequent Legal Update
- For many cash products, adjusted RFRs likely will be acceptable, but especially for bank-provided products – consumer and commercial lending – they may not be
- In the US, this is reflected in the Credit Sensitivity Group, which is arguing for a more risk sensitive alternative to adjusted SOFR, including Ameribor, ICE Bank Yield and a proposed bank CDS index from IHS Markit and, most recently, the proposed "Across-the-curve" (AXI)

LIBOR Transition – Where are we now?

- In the US, the semi-official Alternative Reference Rates Committee (ARRC) has a paced transition plan and has produced a variety of product-specific fallback provisions and general best practices guidance
- The most recent best practices included milestones for discontinuance and transition away from LIBOR starting with floating rate notes by December 31, 2020 and with the last being CLOs by September 30, 2021
- However, there are known issues to complicate the transition, including (1) coordinating cash products and related hedging and (2) so-called “tough legacy” contracts that are unlikely to be remediated due to required consents or difficulty locating affected security holders or other counterparties
- In addition, the transition likely will impose significant strain on systems and personnel

Tough Legacy Contracts

- In response, there are proposed global legislative/regulatory "solutions"
- In the US, the ARRC has proposed a New York legislative solution
  - See our related Legal Update
- In the UK, the Government has promised a legislative "fix"
  - See our related Legal Update
- In the EU, there are proposed revisions to the Benchmark Regulation

And…the SEC Wants to Know About Your LIBOR Transition Preparedness

- The SEC's OCIE has stated that LIBOR preparedness will be an examination priority in 2020
  - See our related Legal Update and Webinar

Americas | Asia | Europe | Middle East

mayerbrown.com