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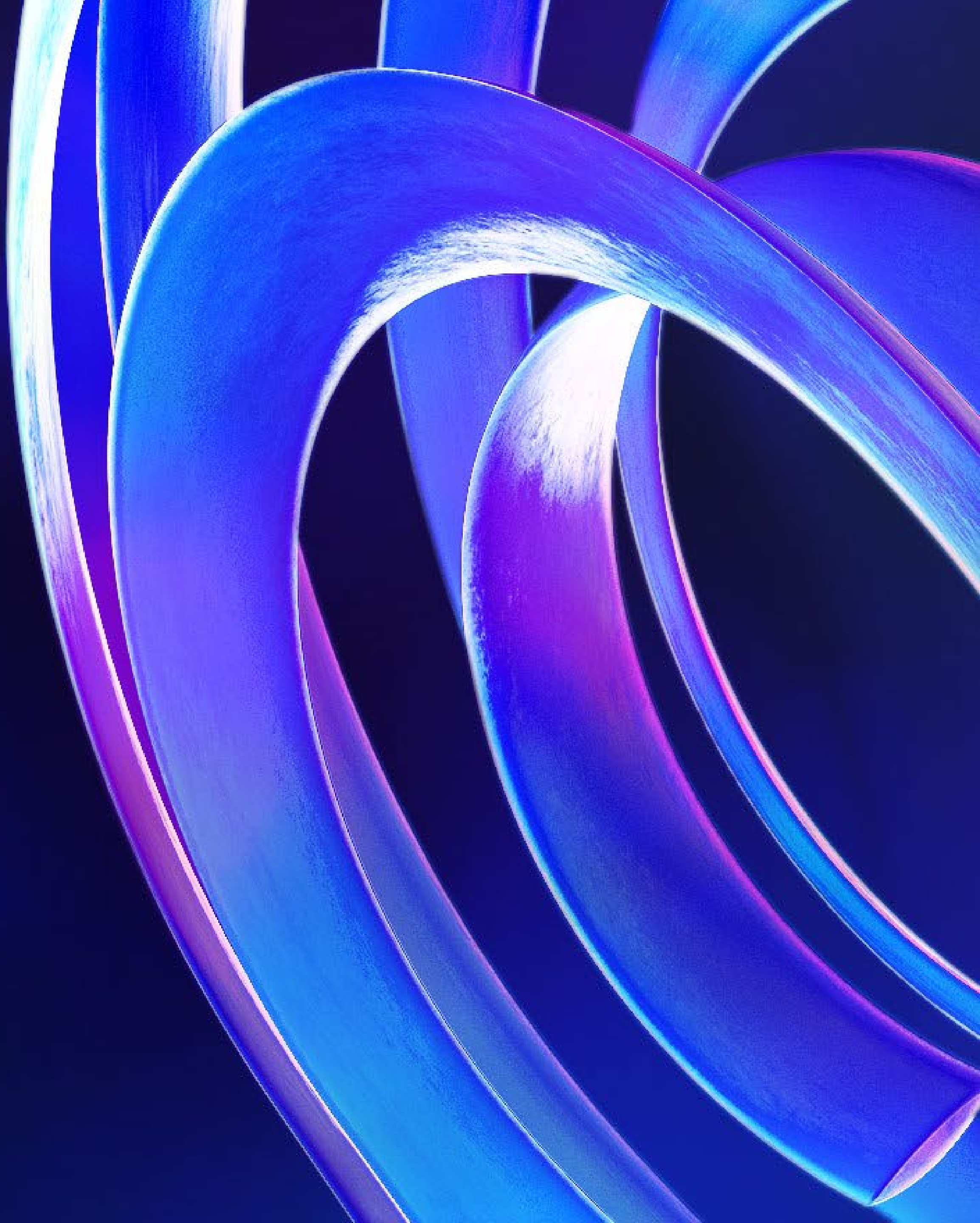
Regulatory Recap

February 2024 at a glance



Regulatory Insights: February 2024 Summary

February regulatory actions span across regulatory intensity/supervision, governance and risk management, consumer/investor protections and tech/data risks, including:

Legend

- Regulatory Intensity
- Governance & Risk Management
- Financial Risk
- Consumer/Investor Protection
- Tech & Data Risks

February

SEC
Denied petition to amend "No-Admit/No-Deny Policy'

CFTC
GMAC recommendations for U.S. Treasury, repo and funding, and commodity markets

DOC
Creates the U.S. AI Safety Institute Consortium (AISIC)

FinCEN
Financial Trend Analysis – convertible virtual currency

NAIC
2024 Strategic Priorities for State Insurance Regulators

CFPB
Supervisory appeals process final rule

FFIEC
Statement on residential lending valuation bias

CFTC
Proposed rule on margin adequacy for FCMs

CFTC
Proposed rule on governance and conflicts of interests for DCMs and SEFs

House
New bipartisan AI task force

Treasury
New sanctions on Russia

White House
Executive Order Access to Bulk Personal Data

FinCEN
Alert on activity in the West Bank

FinCEN
NPR AML risks in the U.S. residential real estate sector

DOJ
National Elder Justice Law Enforcement Summit

FCC
Rules AI-Generated Voices in Robocalls Illegal

SEC, CFTC
Form PF Reporting: Joint Final Rule

FTC
Report: Fraud, Identity Theft, and Other Scams

FinCEN
Proposed rule on AML/CFT requirements for investment advisers

Treasury
Fact Sheet: Actions to Enhance Financial Transparency and Combat Illicit Finance

FTC
Rule on Impersonation of Government and Businesses

FRB
Speech: Supervision with Speed, Force, and Agility

SEC
Final rule defining "Dealers" and "Government Securities Dealers"

DOJ
Designation of first Chief Science and Technology Officer and Chief AI Officer

DOC
NTIA request for comment on open-weight AI models

FINRA
Order routing disclosure final rule

NAIC
Statement on ESG policies

NIST
Cybersecurity Framework V2.0

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Regulatory Perimeter: Expanding Financial Service Coverage

To better identify, assess, and respond to potential risks across financial service markets, regulators are taking actions to "close gaps" in regulatory coverage as well as expand coverage within their supervisory authorities to address market changes. These actions are targeted toward an array of financial services providers (e.g., hedge funds, private equity funds, payment platforms/providers, fintechs), which have grown in both scale and volume spurred on by evolving technological and financial innovations.

Regulators who have recently taken regulatory actions include SEC, FinCEN, CFPB, OCC, FRB and collectively through the FSOC.

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- ***Multi-agency Actions:*** *Acting independently and together through the FSOC, financial services regulators are "closing gaps" in regulatory coverage.*
- ***Existing Authority:*** *Regulators are using existing supervisory authorities to initiate and/or update rulemakings to address market shifts.*
- ***Stability/Systemic Risk Management:*** *Recognizes significant growth in the number and size of an array of financial service providers offering similar products and services and the increasing interconnectedness within the industry.*

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Heightened Risk Standards: Focus on Risk Frameworks, Processes, and Controls

As part of the current focus on heighted risk governance and risk management practices, the financial services sector is experiencing high regulatory intensity in the areas of non-financial risk management, inclusive of a focus on internal controls and operational risk.

In keeping with established prudential regulatory frameworks, financial services regulators expect a company's risk governance framework to fully incorporate policies and standards, credible challenge and demonstrable evidence of dynamic risk assessment in support of the design, effectiveness, and sustainability of risk controls.

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- ***Risk Framework:*** *Heightened regulatory scrutiny built on established prudential risk frameworks and comparisons to 'peers'.*
- ***Risk Governance:*** *Expanded internal controls and non-financial risk management breadth/depth of supervisory and enforcement actions.*
- ***Issues Management:*** *Expectation for enterprise-wide review/application of identified risks to risk assessments/RCSAs, expansion of mitigating controls, and robustness of end-to-end processes.*
- ***Sustainability and Continuous Improvement:*** *Need to demonstrate continuous improvement and sustainability of processes in such areas as internal controls, data management, change management, issues management.*

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Heightened Risk Standards: Focus on Data Management (& BCBS 239)

Regulators are intensifying their scrutiny of financial services companies' data management and data governance practices over risk management data, from aggregation capabilities to internal risk reporting practices. This focus on RDARR (risk data aggregation and risk reporting) is part of the regulators' increasing supervisory and enforcement activities in areas of both financial and non-financial risk.

Financial services companies are expected to demonstrate and sustain elements of "heightened standards" – regardless of size and complexity.

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- ***Governance:*** *Sufficient involvement across the Board, senior management, and three lines of defense in the RDARR framework (e.g., roles/responsibilities, review/challenge; policies, standards, procedures; metrics, risks, controls).*
- ***Data universe and tiering:*** *Adequacy of the scope and breadth of data, metrics, models, reports covered by RDARR, including classification and tiering.*
- ***Data lineage:*** *Ability to trace and report on the relationship between data outputs and business processes, authoritative sources, systems of record, and systems of origin.*
- ***Data management and quality:*** *Standardized processes and controls around access, authorization, use, privacy, security, and sharing; accuracy of data and controls to measure and manage risk exposure and reporting.*

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Heightened Risk Standards: Focus on AML/BSA

With the continuous evolution of sophisticated financial crime patterns, regulators are committed to providing guidance and support for institutions to effectively manage and mitigate financial crime risks. Regulatory focus in areas such as Anti-Money Laundering (AML)/Bank Secrecy Act (BSA)/Countering the Financing of Terrorism (CFT), Know Your Customer (KYC)/Customer Due Diligence (CDD), and transactional activity will continue along with attention to continuously assessing risk and implementing risk-based compliance programs.

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- ***Regulatory Intensity:*** *Expanded AML breadth/depth of supervisory and enforcement actions, risk alerts and evolving BSA, CFT, KYC/CDD regulations.*
- ***Data Lineage and Quality:*** *Focus on traceability of data at both the customer and transaction level, as well as across business processes.*
- ***Transaction Monitoring:*** *Quality of transaction monitoring and surveillance systems, models, processes, and controls, with expectations for increased effectiveness, strength of underlying models, and innovation.*
- ***Expansion of Threats:*** *Expansion of emerging threats and vulnerabilities (e.g., virtual currencies, sanctions evasion, malware/ransomware, and fraud).*
- ***Skills/Talent Matter:*** *Breadth of skills/talent in day-to-day operations of AML reviews, investigations, and escalations; dynamic assessment of staffing needs.*

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Fraud, Identity Theft, and Other Scams

The Federal Trade Commission publishes its 2023 Data Book report outlining information received from consumers regarding their experiences with fraud, identity theft, and other consumer protection-related issues. The annual report is comprised of information the FTC received directly from consumers as well as reports filed with others, including federal, state, and local law enforcement agencies; federal regulatory agencies; industry participants; and non-profit organizations. The information is stored in the FTC's Consumer Sentinel Network (a secure online database that is only available to law enforcement).

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- ***Fraud Losses Increasing.*** *Fraud losses reported in 2023 totaled more than $10 billion, representing a nearly 14 percent increase over reported fraud losses in 2022.*
- ***Identity Theft Tops Concerns****. Consistent with 2022, Identity Theft was the most commonly reported complaint in 2023.*
- ***Reported Payment Method.*** *The highest reported fraud losses (where a payment method was identified) were associated with bank transfers and payments and cryptocurrencies.*

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NAIC 2024 Strategic Priorities for State Insurance Regulators

The National Association of Insurance Commissioners announces its strategic priorities for 2024. The priorities aim to pursue "innovative and effective solutions to the most pressing issues affecting consumers, the insurance sector, and markets". Priorities include:

- Climate Risk/Natural Catastrophes and Resiliency
- Insurer Financial Oversight and Transparency
- Marketing of Insurance Products
- Race and Insurance, Financial Inclusion, and Protection Gaps
- Use of AI by Insurers and Cyber Risks

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- ***Regulatory "Roadmap":*** *The NAIC's 2024 strategic priorities provide a regulatory "roadmap" for companies to gain insight into areas of upcoming insurance-related regulatory risk and attention.*
- ***Common Themes:*** *NAIC priorities align to both its 2023 priorities but also to other financial service regulators, including climate, fair marketing, consumer protections, AI/predictive models and cybersecurity.*

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Financial Crimes & AML: FinCEN Proposal and Treasury Actions

Furthering efforts to combat illicit finance threats, vulnerabilities, and risks, the Department of the Treasury and its Financial Crimes Enforcement Network each take action, including:

- A FinCEN proposal to “keep criminals and foreign adversaries from exploiting the U.S. financial system and assets through investment advisers.”
- Four Treasury Risk Assessment reports, including one for the investment adviser sector, which provide updated information on the illicit finance environment and changes to the AML/CFT framework.

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- ***“Closing the Gap”:*** *Expanding regulatory perimeter to “close the gap” in regulatory coverage and further mitigate potentially illicit finance risks through the investment adviser industry, including advisers to private funds.*
- ***AML/CFT/BSA Focus:*** *Expanding breadth/depth of supervisory, enforcement, and evolving regulatory expectations focused on AML/CFT/BSA requirements aligned with emerging threats and vulnerabilities (e.g., beneficial ownership reporting, CDD).*
- ***National Security Ties:*** *Treasury risk assessments identify illicit finance risks as a “common thread” across threats to national security.*

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Form PF Reporting: SEC, CFTC Joint Final Rule

The Securities and Exchange Commission and the Commodity Futures Trading Commission jointly adopt a final rule to amend Form PF “largely as proposed”. The final rule expands the reporting requirements for certain SEC-registered investment advisers to private funds that are also registered with the CFTC as a commodity pool operator or commodity trading adviser. According to the Commissions, the adopted amendments aim to enhance the ability of the Financial Stability Oversight Council to monitor and assess systemic risk as well as “strengthen the effectiveness of the SEC's regulatory programs, including examinations, investigations, and investor protection efforts relating to private fund advisers.”

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- ***Expanding Private Fund Coverage:*** *Continued increasing regulatory requirements to the private fund market (including hedge fund advisers) to increase transparency in terms of investment exposure, positions, and borrowing/financing arrangements.*
- ***Stability/Systemic Risk Management:*** *Form PF rules intended to fill “information gaps” that may help the SEC, CFTC and FSOC better understand and identify financial stability and systemic risks.*
- ***Additional Regulatory Scrutiny:*** *Expect enhanced private fund scrutiny of compliance to new rulemaking, insider trading/conflicts of interest, risk management/controls and risk governance.*

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Dealer Definition: SEC Final Amendments

The Securities and Exchange Commission adopted new rules 3a5-4 and 3a44-2 under the Securities Exchange Act of 1934 (first proposed in March 2022), which apply to any person with control of over $50 million of total assets engaging in liquidity-providing roles “as part of regular business” (e.g., persons who are engaged in a regular pattern of buying and selling securities that has the effect of providing liquidity to other market participants, including proprietary or principal trading firms, private funds, and registered investment advisers).

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- ***Expanded Regulatory Perimeter:*** *Expansion of regulatory registration and supervisory coverage to traders and hedge funds (e.g., SRO, proprietary traders) who engage in liquidity-providing roles “as part of regular business”.*
- ***Non-Exhaustive:*** *Recognition that while not all circumstances may be covered in the final rules, the final rule will still apply if acting as a dealer or government securities dealer.*
- ***Low Threshold:*** *Applies to any person with control of over $50 million of total assets.*

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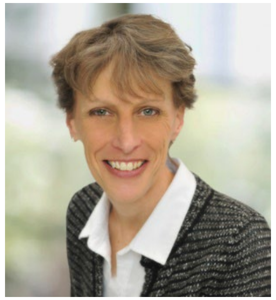

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