Investment Services Regulatory Update

August 2025

Monthly Version

VedderPrice

LITIGATION DEVELOPMENTS

D.C. Circuit Court Upholds Ruling that Proxy Voting Advice Is Not Solicitation

On July 1, 2025, the U.S. Court of Appeals for the District of Columbia Circuit upheld the February 23, 2024 judgment of the U.S. District Court for the District of Columbia that proxy voting advice does not constitute "solicitation" for purposes of Section 14(a) of the Securities Exchange Act of 1934 and related proxy rules.

From 2019 through July 2022,[1] the SEC issued interpretations and guidance regarding, and adopted amendments to, the proxy rules under the Exchange Act that extended the definition of "solicit" and "solicitation" to expressly include the furnishing of proxy voting advice for a fee, thereby extending the antifraud provisions of Rule 14a-9 under the Exchange Act to apply to proxy voting recommendations offered by proxy advisory firms. According to the SEC, because proxy advisory firms market their expertise in, and receive fees for, researching and analyzing matters submitted to a shareholder vote and providing voting recommendations, those recommendations are reasonably calculated to influence votes and should be considered a solicitation regardless of whether the recommendations are followed. In response, a proxy advisory firm filed suit contesting the SEC's extension of the proxy rules to proxy voting advice, claiming that proxy advisory firms do not "solicit" proxies because proxy advisory firms "do not seek proxy authority or ask shareholders to vote a certain way to achieve a particular outcome." On February 23, 2024, the U.S. District Court for the District of Columbia granted summary judgment for the proxy advisory firm and vacated certain of the SEC's proxy rule amendments, holding that "the ordinary meaning of 'solicit' at the time of Section 14(a)'s enactment does not reach proxy voting advice for a fee" and therefore, by defining "solicit" and "solicitation" in such a way, "the SEC acted contrary to law and in excess of statutory authority."

The SEC and the National Association of Manufacturers (NAM) appealed the District Court's ruling. Subsequently, in August 2024 the SEC dismissed its appeal leaving NAM as the sole appellant defending the definitional change in the amended rule. The D.C. Circuit reviewed the District Court's grant of summary judgement *de novo* and affirmed the District Court's ruling. The Circuit Court held that the ordinary meaning of "solicit" for purposes of Section 14(a) of the Exchange Act "refers to a request for proxy authority or a directed plea to exercise such authority in a particular manner" and that proxy voting advice "rendered by a third party for a fee falls outside that definition" and is "simply a recommendation." The Circuit Court further held that the SEC's effort to expand the definition of "solicitation" to include proxy voting advice cannot be reconciled with the text of Section 14(a) and such effort was contrary to law.

The opinion of the U.S. Court of Appeals for the District of Columbia Circuit is available here.

[1]Attorneys in Vedder Price's Investment Services group previously published articles on the SEC's August 2019 guidance, November 2019 proposing release, July 2020 adopting release, and July 2022 adopting release.

U.S. Supreme Court Takes Up Circuit Split Regarding Investment Company Act Private Right of Action Asserted by Closed-End Fund Activists

On June 30, 2025, the U.S. Supreme Court granted certiorari in *FS Credit Opportunities Corp. v. Saba Capital Master Fund, Ltd.*[1] in order to resolve a split among U.S. Circuit Courts of Appeals regarding whether Section 47(b) of the Investment Company Act of 1940 creates an implied private right of action to rescind contracts for alleged violations of any provision of the Investment Company Act. Generally, only the SEC has the authority to enforce the Investment Company Act, with the exception of Section 36(b) of the Investment Company Act which expressly establishes a private right of action that allows shareholders of a registered fund to bring suits, on behalf of the fund, alleging breaches of fiduciary duty with respect to compensation paid by the fund or its shareholders to the fund's investment adviser or its affiliates. While several Circuit Courts, including the Third and Ninth Circuit Courts, have previously held that Section 47(b) does not create an implied private right of action, in 2019 the Second Circuit

Court of Appeals in *Oxford University Bank v. Lansuppe Feeder, LLC* held that Section 47(b) provides an implied private right of action.

Section 47(b) of the Investment Company Act provides, in relevant part, that:

> (1) A contract that is made, or whose performance involves, a violation of [the Investment Company Act]…is unenforceable by either party…(2) To the extent that a contract described in paragraph (1) has been performed, a court may not deny rescission at the instance of any party unless such court finds that under the circumstances the denial of rescission would produce a more equitable result than its grant and would not be inconsistent with the purposes of [the Investment Company Act].

Since the *Oxford University Bank* decision, closed-end fund activist investors have sued numerous registered closed-end funds under Section 47(b) in an effort to rescind certain of the funds' anti-takeover measures, including opting into state control share statutes (*e.g.*, the Maryland Control Share Acquisition Act (MCSAA)) and requiring a majority instead of a plurality vote in contested director elections, claiming that such measures affect a contractual relationship with fund shareholders.

FS Credit Opportunities Corp. involves closed-end funds registered under the Investment Company Act and organized under Maryland law. As an anti-takeover measure, each fund's board adopted resolutions opting into the MCSAA, thereby limiting the ability of fund shareholders to vote their shares to the extent their ownership of fund shares exceeded a certain threshold. This measure limited the ability of activist investors owning a large number of shares to affect director elections and take control of the funds' boards. Saba, an activist investor in the funds, sued the funds in the U.S. District Court for the Southern District of New York, seeking rescission of the control share resolutions pursuant to Section 47(b) of the Investment Company Act. Saba alleged that in opting into the MCSAA, the funds violated Section 18(i) of the Investment Company Act, which provides that "every share of stock…issued by a registered management company… shall be a voting stock and have equal voting rights with every other outstanding voting stock …" The U.S. District Court for the Southern District of New York, citing *Oxford University Bank*, granted summary judgment in favor of Saba and ordered the rescission of the control share resolutions. On appeal, the Second Circuit affirmed the decision of the District Court.

The Investment Company Institute (ICI) submitted an *amicus curiae* brief in support of the petition for certiorari, arguing that "[t]he availability of a private right of action under Section 47(b)…risks upending the long-established regulatory structure governing the registered fund industry, causing significant regulatory uncertainty and wasteful litigation." Noting that the Investment Company Act granted sole enforcement authority to the SEC, the ICI warned that a private right of action to enforce substantive provisions of the Investment Company Act could result in a "flood of new litigation" and lead to interpretations of the Act in conflict with those of the SEC upon which registered funds and their boards rely.

The Supreme Court docket, which includes the funds' petition for writ of certiorari and the ICI's *amicus curiae* brief, is available here.

[1]See Supreme Court No. 24-345.

ENFORCEMENT DEVELOPMENTS

SEC Agrees to Dismiss First Liquidity Rule Enforcement Action

On July 11, 2025, the SEC announced the filing of a joint stipulation in the U.S. District Court for the Northern District of New York, agreeing to dismiss, with prejudice, its first-ever enforcement action under Rule 22e-4 under the Investment Company Act of 1940, the SEC's liquidity rule. The SEC filed the complaint on May 5, 2023 against a registered mutual fund's investment adviser, the fund's two independent trustees and the two fund officers responsible for implementing the fund's liquidity risk management program pursuant to the liquidity rule, alleging that the defendants aided and abetted the fund's violations of the liquidity rule. In its litigation release announcing the joint stipulation, the SEC stated that it had determined that the dismissal of this action was appropriate "in the exercise of its discretion and as a policy matter."

The foundation of the SEC's enforcement action was the fund's alleged investment in shares of a private company that constituted approximately 21% to 26% of the fund's net assets during the relevant period and the alleged misclassification of such shares as "less liquid investments," rather than "illiquid investments," under the liquidity rule. The liquidity rule limits the amount of illiquid investments a mutual fund can hold to 15% of its net assets, and exceedances of this limit trigger certain board reporting and SEC filing requirements. The SEC alleged that the fund's investment adviser, as the administrator of the fund's liquidity risk management program, and the two fund officers responsible for implementing the program classified the investments as "less liquid investments" without a reasonable basis to support such classification and against the advice of fund counsel and the view of the fund's external auditors. The SEC also alleged that the fund's trustees allowed the fund to make such classification and failed to exercise reasonable oversight.

The defendants moved to dismiss the case on July 11, 2023, arguing that the liquidity rule exceeds the scope of the SEC's rulemaking authority under the Investment Company Act and is unenforceable. On March 27, 2025, the court denied the defendants' motions to dismiss with leave to refile their motions to provide additional briefing to address the U.S. Supreme Court's recent decision in *Loper Bright Enterprises v. Raimundo* (June 28, 2024), in which the Court overruled the broad deference courts previously afforded to an agency interpretation of a statute administered by that agency, as established in *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.* The defendants refiled their motions to dismiss on April 28, 2025 in light of *Loper*, and following the additional briefing, the SEC agreed to dismiss the action with prejudice, which means the SEC cannot refile the charges.

The SEC's litigation release is available here.

SEC Settles Charges Against Fund Advisers and Portfolio Managers for Alleged Misrepresentations of Risk and Breaches of Fiduciary Duty

On June 30, 2025, the SEC announced it had obtained final judgments in federal district court in a lawsuit brought against two affiliated investment advisers and their two portfolio managers for breaches of fiduciary duty and material misrepresentations relating to their risk management practices and risks of options strategies employed for a registered mutual fund and several private funds, which collectively incurred losses of over $1 billion in February 2018. Each of the defendant advisers and portfolio managers consented to the entry of the applicable final judgment without admitting or denying the allegations in the SEC's complaint.

According to the SEC's complaint filed on May 27, 2021, the advisers employed "short options" or "short volatility" trading strategies for the funds, consisting of writing (selling) short-dated, out-of-the-money options on S&P 500 futures contracts, designed to hedge against declines in the S&P 500 futures market and to benefit from higher volatility market environments. The advisers offered these strategies in three variants, available in the mutual fund, the private funds and/or a separately-managed account,

which differed in the targeted range of returns and amount of hedging provided. In communications to investors and financial advisers as well as to the mutual fund board, the defendants made various representations regarding the risk management practices employed for the funds, including that the funds' portfolios were stress tested against historic market events and that the funds were managed to maintain a consistent level of portfolio risk regardless of market conditions. The defendants also disclosed to investors and financial advisers worst-case loss estimates for each variant of the options strategy. The SEC alleged that such worst-case loss estimates "were false" and "were neither based on, nor consistent with, any stress testing performed by [the advisers] based on historical market scenarios" and that such stress testing projected losses for the funds that were "significantly larger" than the estimates disclosed to investors. Additionally, the defendants made representations regarding their risk management practices, including with respect to their utilization of daily risk reporting, to the mutual fund board in connection with the advisory contract renewal process pursuant to Section 15(c) of the Investment Company Act of 1940, which the SEC alleged were false and misleading.

According to the SEC's complaint, from late 2017 to early 2018, during a low volatility environment, the defendants, in seeking to achieve greater returns, made investments that significantly increased the risk of loss in the funds, while disclosing to investors that they were maintaining consistent risk profiles for the funds. In early February 2018, the S&P 500 Index fell more than 6% and the CBOE Volatility Index increased 177% over two consecutive trading days. As a result, in order to comply with margin requirements imposed by the futures commission merchant for the funds, the funds incurred trading losses of more than $1 billion, or approximately 80% of their value.

The final judgments permanently enjoined each of the defendants from violations of various antifraud provisions of the federal securities laws, among other related violations cited in the judgments. In addition to ordering disgorgement of profits with prejudgment interest, the final judgments imposed $500,000 and $200,000 civil penalties, respectively, on the two portfolio managers and enjoined them for three years and one year, respectively, from managing or advising on securities investments for, or acting as or being associated with an investment adviser to, any third party, except for their wives and children. The SEC's litigation release announcing the final judgments is available here. The SEC's original complaint is available here.

NEW AND PROPOSED RULES

FinCEN Postpones Effective Date of Investment Adviser Anti-Money Laundering Requirements

On July 21, 2025, the U.S. Department of the Treasury's Financial Crimes Enforcement Network (FinCEN) announced its intention to postpone by two years the effective date of the final rule that it adopted on August 28, 2024 which adds registered investment advisers (RIAs) and exempt reporting advisers (ERAs) to the definition of "financial institution" under the Bank Secrecy Act. The final rule thereby extends certain anti-money laundering/countering the financing of terrorism (AML/CFT) program requirements to these advisers, requiring them to develop and implement a written AML/CFT program that is risk-based and reasonably designed to prevent the adviser from being used for money laundering, terrorist financing or other illicit finance activities. The final rule would have become effective, and compliance with the final rule would have been required by, January 1, 2026; however, FinCEN intends to postpone this to January 1, 2028.

The announcement of the final rule's postponed effective date states:

> FinCEN recognizes…that the rule must be effectively tailored to the diverse business models and risk profiles of the investment adviser sector. FinCEN also recognizes that extending the effective date of the rule may help ease potential compliance costs for industry and reduce regulatory uncertainty while FinCEN undertakes a broader review of the [rule].

The announcement also states that during the postponement period, FinCEN intends to revisit the substance of the final rule through a future rulemaking process.

In addition, FinCEN intends, together with the SEC, to revisit their May 13, 2024 jointly proposed rule under the Bank Secrecy Act that would impose new customer identification program (CIP) requirements on RIAs and ERAs. Under the joint proposed rule, advisers would be required to establish, document and maintain written CIPs as part of their overall AML/CFT programs.

The Treasury Department's announcement is available here.

GUIDANCE AND OTHER DEVELOPMENTS

SEC Division of Corporation Finance Staff Issues Guidance on Disclosure Requirements for Crypto Asset Exchange-Traded Products

On July 1, 2025, the staff of the SEC's Division of Corporation Finance issued a statement providing the staff's views on the application of certain disclosure requirements under the Securities Act of 1933 and the Securities Exchange Act of 1934 to offerings of crypto asset investment products listed and traded on national securities exchanges (crypto asset ETPs). Crypto asset ETPs are typically structured as trusts that hold assets consisting of spot crypto assets or derivative instruments that reference crypto assets. The statement reflects the staff's observations regarding crypto asset ETP disclosures and provides the staff's views on questions received from market participants. The staff's statement does not address crypto asset ETPs registered under the Investment Company Act of 1940.

The staff's statement addresses a broad array of disclosure topics, including the prospectus cover page; prospectus summary; risk factors; underlying assets; pricing and NAV calculation; service providers; custody; fees and expenses; description of securities issued and voting rights; distribution; directors, executive officers and significant employees; conflicts of interest; and financial statements. Crypto asset ETP issuers also should consider whether they are permitted to provide "scaled disclosure" with respect to any applicable disclosure requirements—less extensive disclosure that is sometimes applicable to smaller reporting companies, non-accelerated filers, or emerging growth companies.

The staff notes that its statement does not address all material disclosure items and that the disclosure topics it does address may not be relevant for all issuers. To that end, issuers are reminded to consider their own facts and circumstances, tailor their disclosures accordingly, and avoid generic or boilerplate disclosures. The staff emphasizes that disclosure should be presented in clear, concise, and understandable language, without overly relying on technical terminology or jargon.

The staff's statement is available here.

The staff's statement represents a continuation of its ongoing effort to provide greater clarity on the application of the federal securities laws to crypto assets, which Vedder Price has previously summarized here.

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