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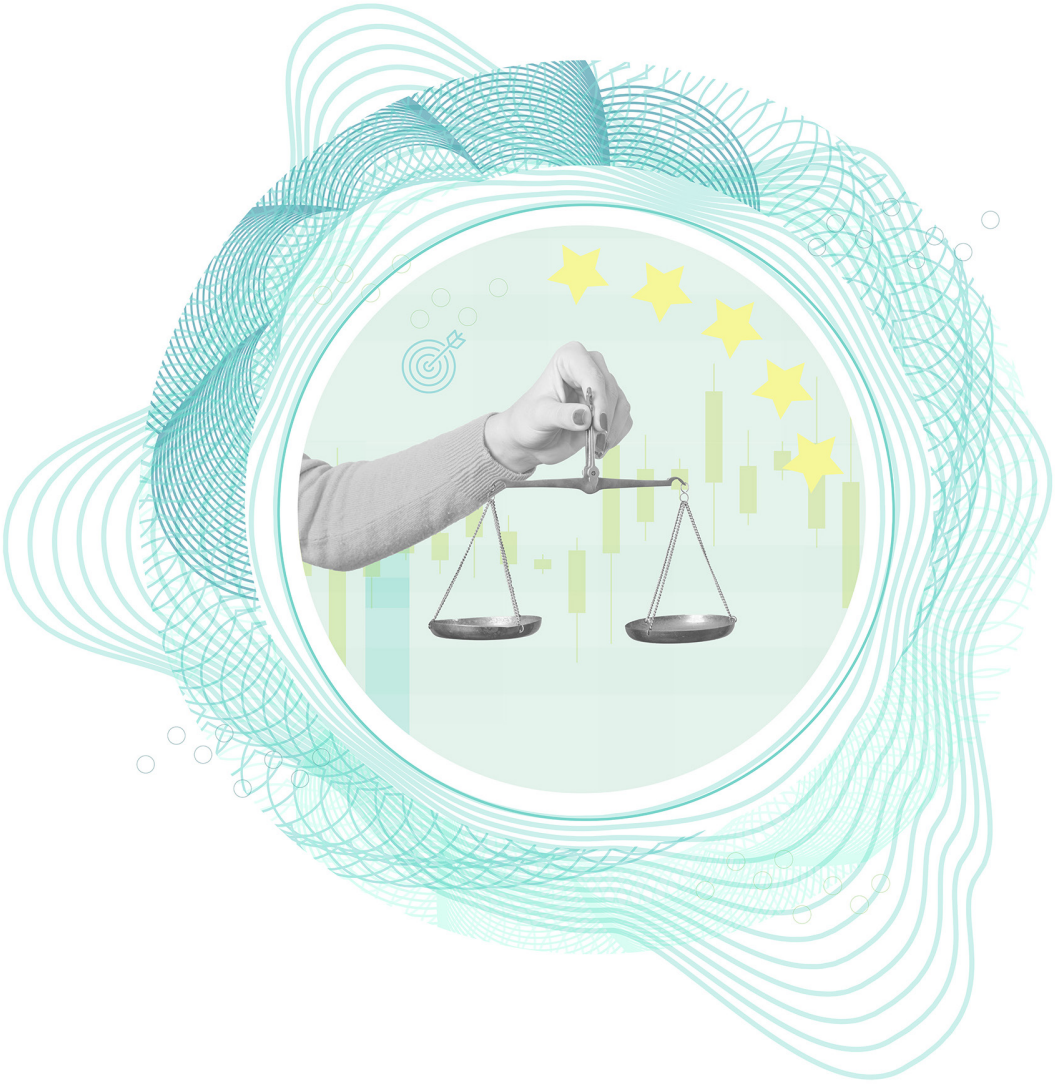

2022 investment management regulatory outlook

Meet impending deadlines while keeping an eye toward new developments

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Introduction

2022 includes several important compliance deadlines and the likelihood that significant new regulations impacting the investment management space will be proposed as federal agencies, like the Securities and Exchange Commission (SEC), transition from a planning period to an execution phase. The second half of 2022 will see new SEC Rules 2-5 and 18f-4 become effective, as well as amendments to Rule 206(4)-1. Beyond compliance deadlines, firms should consider areas where regulatory action is accelerating or emerging including cyber risk; climate finance; diversity, equity, and inclusion (DEI); and digital assets. We expect regulatory activity in each of these areas in 2022.[1]

We've categorized each of this year's topics as either foundational, evolving, or emerging. Foundational topics are those where regulations have been finalized and firms are working to meet 2022 compliance deadlines. Evolving topics are those where amended regulations have been proposed or new guidance has been issued. Emerging topics are those where regulatory activity is underway, but uncertainty about the future of the regulatory framework remains.

The expanding regulatory perimeter

Across all sectors, we expect to see continued extension of the regulatory perimeter in 2022. While 2021 served as a year for the Biden administration to settle into governing, 2022 will be an opportunity to fill remaining key vacancies, which will allow the agencies to better fulfill their regulatory missions. There are frontier topics like climate finance and digital assets that are top of mind for many, but regulatory expansion is not limited to these areas. Foundational regulations are being tested not only by new technologies but also by new business models. As industries evolve and the lines between them blur, regulators increasingly feel that their entity-based frameworks are not sufficient to address emerging risks. They have even gone as far as enlisting Congress to bolster their authority in rapidly evolving areas.[2]

To the extent possible, they are also shifting their focus to activities and testing the limits of their authority. Horizontal integration and new business models have created an opening for financial regulators to wield some authority in industries that were not traditionally in their purview (namely, tech). Nevertheless, the agencies wish to address coming challenges proactively rather than reactively and as such, we expect them to move the needle substantially in 2022 in the areas of digital assets, ESG investing and cybersecurity, among others. Despite the activities focus, certain firms may face a barrage of challenges ranging from agency rulemaking and enforcement, to renewed enthusiasm for antitrust pursuits, to possible legislation.

In the area of climate policy, the specter of climate stress tests and scenarios analysis looms large for financial institutions. However, ESG disclosure standards, which the SEC continues to promise, have the potential to impact every public company regardless of industry. Although it is a volatile and even more arduous process than agency rulemaking, legislation remains a wild card that could accelerate the current trajectory.

Firms should expect to devote more attention and more resources to regulatory changes in 2022 and beyond. Attempts by US regulators to "catch up" with their counterparts in Europe and elsewhere present a challenge not only to firms but the regulatory agencies as well. Thus, the present moment is ideal for engagement with policymakers; rather than deny the conversation, firms should seek to inform it.

Foundational regulatory topics

Derivatives

Starting August 19, 2022, funds will be required to comply with Rule 18f-4 under the Investment Company Act of 1940, as adopted by the SEC, which governs senior securities, including derivatives transactions by registered investment companies and business development companies (BDCs).[3] The 18f-4 rule modernizes the current regulatory regime with respect to derivatives transactions and serves to rescind Release IC-10666 and related regulatory guidance. By the first quarter of 2022, firms should be well underway to determining their rule readiness and implementation plans. In this regard, one of the first actions firms should consider taking is to evaluate and select the Derivatives Risk Manager (DRM), who will be responsible for administering the Derivatives Risk Management Program (DRMP), as set forth in 18f-4. DRMs should be involved in the initial stages of rule implementation, if possible, and must be formally approved by the fund's board prior to the August 19 compliance date. DRMs will be responsible for providing periodic board reporting and will serve as the primary escalation point for certain risk-related events.

Firms should also be in the process of drafting and implementing a written DRMP, which according to the rule must be formally adopted.

Firms should also be in the process of drafting and implementing a written DRMP, which according to the rule must be formally adopted. The DRMP is required to have policies focused on identifying and assessing risks associated with each fund's derivatives transactions and should set forth risk guidelines for measuring those risks. Firms should consider developing a risk matrix or lexicon that includes a list of each fund's derivatives use, risks associated with each derivative (e.g., counterparty risk, leverage risk), and how those risks are to be measured and monitored (e.g., credit valuation adjustment). The DRMP should also address parameters related to stress testing and back-testing, and should establish protocols for measuring, monitoring, and enforcing limits based on value at risk (VaR). In addition, the rule requires that a fund's VaR be measured using the relative VaR test, unless it is determined that the absolute VaR test is more appropriate, in which case the decision should be documented. The DRMP should also include calculation methodologies that will be used for VaR testing (e.g., Monte Carlo, historical, parametric). For funds using relative VaR testing, a designated reference portfolio must be selected.

Finally, some funds might be considered limited derivatives users (LDUs) and, as such, will not be required to comply with the full rule; however, in order to use this exception, certain thresholds related to derivatives must be met (e.g., derivatives should be less than 10% of the fund's net assets). In this regard, firms should consider implementing soft limits (e.g., <5%) to ensure the <10% threshold is not inadvertently breached. For funds that might consistently breach the <10% threshold, firms should consider including them in the full compliance program. The rule also permits funds (other than money market funds) to enter into certain other transactions (e.g., reverse repurchase agreements) provided that the asset coverage requirements of section 18 are complied with (or that all reverse repurchase agreements or similar financing transactions are treated as derivatives). Firms should carefully consider if they will categorize all reverse repurchase agreements as derivatives, especially given the need to maintain compliance with LDUs' <10% threshold.

The rule also permits money market funds (as well as other fund types) to invest in securities settling on a when-issued, forward-settling, or non-standard basis provided that a "T+35" settlement time frame is met. Firms should have the ability to monitor all transactions (e.g., term loans) that might settle outside the 35-day window and thus would not be able to meet the rule's extended settlement provisions. Also, firms will be required to enhance certain disclosure requirements, such as the filing of Form N-RN, Form N-PORT, and Form N-CEN.

Given the tight timeline to comply with the rule, firms should already be in the process of understanding the rule's widespread impacts to their business operations (e.g., risk, compliance, information technology) to ensure compliance can be achieved by the August 19 deadline.

Fair valuation

Starting on September 8, 2022, funds will be required to comply with Rule 2a-5 under the Investment Company Act of 1940, as adopted by the SEC. Rule 2a-5 is designed to provide funds' boards of directors and registered investment advisers with a consistent, modern approach to making fair value determinations across all mutual fund groups, including BDCs. Rule 2a-5 clarified that the definition of "readily available market quotations" is limited to investments priced via reliable, unadjusted quoted prices in active markets. All other investments valued have been deemed to be fair valued.

In addition, 87% of survey respondents said they had not yet defined what constitutes a material valuation risk, and 68% have not finished documenting their key valuation inputs and assumptions. The industry's challenges in developing a comprehensive risk assessment and management framework are characterized by the lack of a standard and consistent approach and criteria for identifying material valuation risks (which might include—among other things—sources of conflicts of interest, bifurcation of assets in risk categories, valuation model risks, portfolio valuation uncertainty, and valuation continuity risks).

In developing a road map and solutions toward rule compliance, a key focus is having a standardized methodology and testing approach, including a set of acceptable thresholds across all valuation sources.

While the impact on boards will vary by mutual fund group, Rule 2a-5 expressly permits each board to designate the determination process to a valuation designee, typically the investment adviser. Rule 2a-5 requires an active oversight model that requires boards to oversee the:

- Assessment and management of **valuation risks**
- Establishment and consistent application and testing of **fair value methodologies**
- Evaluation and oversight of **pricing services**

This is something we have seen evolve over time through the lens of data and trends captured in the Deloitte Fair Valuation Pricing Survey.[4] According to our most recent survey, the assessment and management of valuation risk required by Rule 2a-5 will be a significant focus of implementation efforts. Specifically, 67% of survey participants identified this area as a gap in current practices, and 65% identified it as the aspect of Rule 2a-5 that will most challenge the current valuation process. Although Rule 2a-5 does not specify which risks need to be addressed, the SEC did provide a "non-exhaustive" list of valuation risks that many boards and valuation designees are considering as a starting point for developing a valuation risk assessment framework.[5]

Another key challenge is evaluating and testing the appropriateness and accuracy of fair value methodologies, with 40% of survey participants citing it as a gap. In developing a road map and solutions toward rule compliance, a key focus is having a standardized methodology and testing approach, including a set of acceptable thresholds across all valuation sources.

With the compliance deadline looming, it's important for mutual fund groups to understand Rule 2a-5's impacts on key aspects of their business operations, including risk, compliance, and information technology. Leading practice suggests that working groups should be established and tasked with managing the nuances of Rule 2a-5 compliance, including gap and valuation risk assessment; evaluation of testing methods; board reporting; and oversight and monitoring of third-party pricing data sources.

Modernization of investment adviser marketing

Entering 2022, advisers that have not already done so will need to start aligning their advertising and marketing practices to meet the requirements of amended Rule 206(4)-1 under the Investment Advisers Act of 1940, as adopted by the SEC. The amendments went into effect on May 4, 2021, and have a compliance date of November 4, 2022. Among other things, amended Rule 206(4)-1 updated the definition of "advertisement" to include communications to investors (both existing and prospective) and private funds.

When implementing the new definition, advisers need to pay close attention to the precise scope of the rule, which covers any direct or indirect communications offering investment advisory services to more than one person (as well as communications to just one person if the material includes hypothetical performance). The rule also covers communications offering new services to existing clients, as well as any endorsement or testimonial for which an adviser receives direct or indirect cash and non-cash compensation.

- Providing testimonials, **endorsements**, and third-party ratings, unless the adviser satisfies certain disclosure, oversight, and disqualification provisions (as well as criteria pertaining to the preparation of the rating)

Since adoption of Rule 206(4)-1, advisers have been assessing its impact on their advertising and marketing practices. One key challenge has been navigating how the rule's specific provisions related to the use of investment performance information intersect with the Global Investment Performance Standards (GIPS®).[6] Advisers that are GIPS-compliant should be mindful of how the rule will affect their investment performance reporting. GIPS reports are generally standardized and include information that is not customized (e.g., composite-level information). As such, they will likely be viewed as advertising and will be subject to the rule.

There are a number of similarities between Rule 206(4)-1's requirements and requirements under the GIPS standards. In fact, the adopting release to the rule cites the GIPS standards in a number of instances. As such,

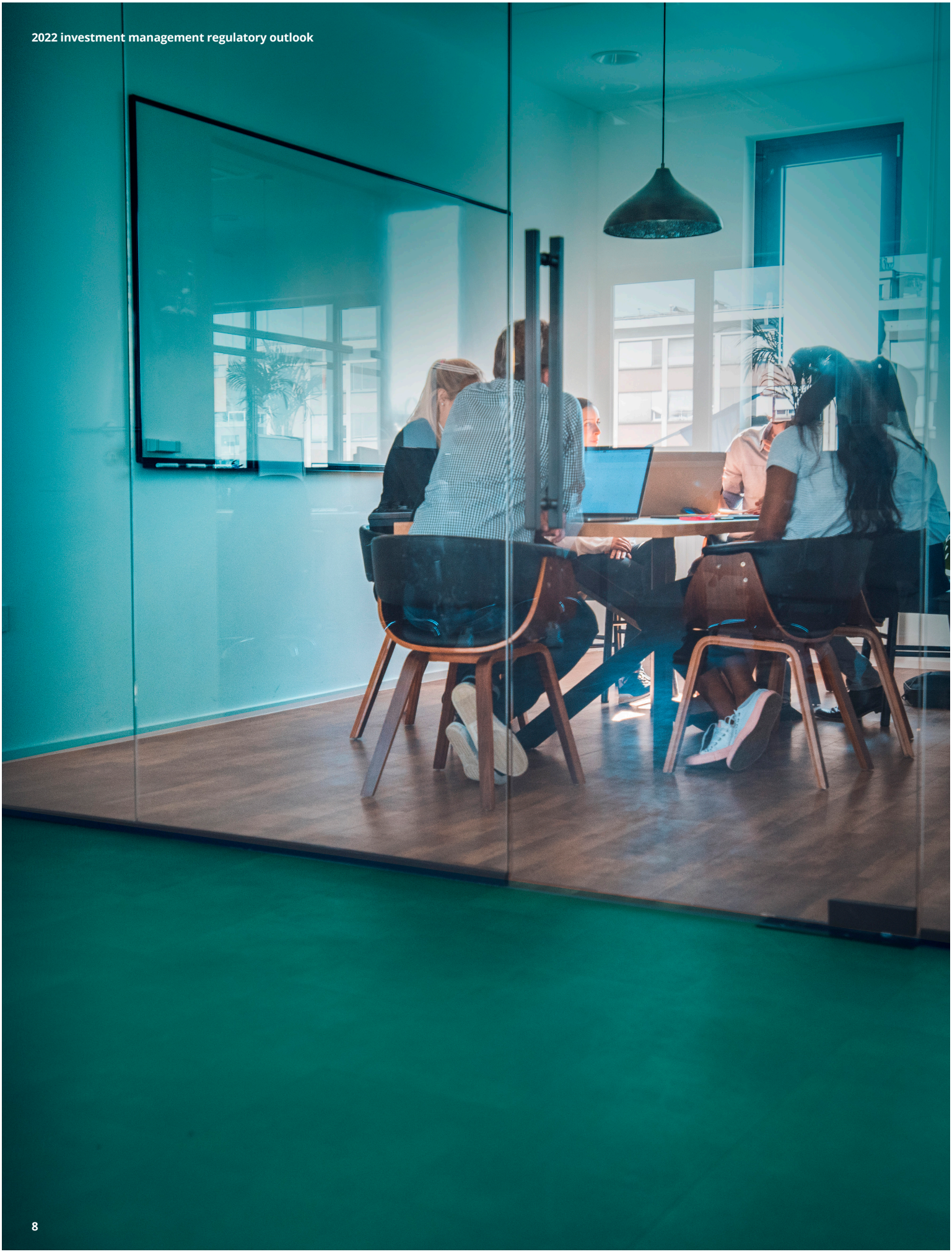
Under Rule 206(4)-1, there is a general prohibition of certain marketing practices to prevent fraudulent, deceptive, or manipulative acts.

Under the rule, there is a general prohibition of certain marketing practices to prevent fraudulent, deceptive, or manipulative acts. These include:

- Making statements of material fact with information that would be **untrue or omits** a material fact
- Discussing any potential benefits **without providing fair and balanced treatment** of associated material risks or limitations
- Making a material statement of fact that the adviser might not be able to **substantiate** upon demand by the SEC
- Referencing specific **investment advice** provided by the adviser that is not presented in a fair and balanced manner
- Including or excluding **performance results**, or presenting time periods, in a manner that is not fair and balanced

GIPS-compliant firms will likely have an easier time complying with certain rule requirements related to investment performance. However, there are a handful of distinct differences that in some cases will conflict, requiring advisers to pay particular attention to their current practices and those that might need to change. Firms that have yet to adopt the GIPS standards might find this an opportune time to pursue compliance, with the standards offering a framework to follow that aligns with certain Rule 206(4)-1 requirements related to investment performance.

For advisers in 2022, aligning their advertising and marketing procedures with the amended rule will likely require revising policies and procedures, expanding compliance oversight of marketing practices, and appropriately identifying the scope of advertisements. Also, GIPS-compliant firms will likely need to assess their existing GIPS practices to ensure they are compliant with the rule's requirements.



Evolving regulatory topics

Cyber, fraud, and financial crime

The increased rate of digital transformation that US financial institutions (FIs) undertook during the pandemic and through 2021 has brought its own set of security challenges and risks. According to Federal Reserve Chairman Jerome Powell, cyberattacks are now the foremost risk to the global financial system, even more than the lending and liquidity risks that led to the 2008 financial crisis.[7] A report by the International Criminal Police Organization (INTERPOL) showed an alarming rate of cyberattacks during the pandemic with a significant target shift from individuals and small businesses to major corporations, governments, and critical infrastructure.

On June 30, 2021, the Federal Financial Institutions Examination Council (FFIEC) published the "Architecture, Infrastructure, and Operations" booklet of the FFIEC Information Technology Examination Handbook, which supersedes the "Operations" booklet published in 2004.[8] To promote safety and soundness, the booklet emphasizes the interconnectedness between a FI's assets, processes, and third-party service providers.

The booklet reflects the overall view that financial institutions are both responsible and need to demonstrate a level of capability to effectively identify and address IT risks that affect their business models, with an emphasis on Governance. There is an expectation that FIs will:

- Define the responsibilities of **key IT executive** roles
- Provide **oversight of third-party** service providers, which is newly introduced in this booklet considering many entities are outsourcing AIO activities to one or more third-party service providers (including cloud service providers)

According to Federal Reserve Chairman Jerome Powell, cyberattacks are now the foremost risk to the global financial system, even more than the lending and liquidity risks that led to the 2008 financial crisis.[7]

To align with rapidly changing and evolving technologies in the financial markets, the booklet also incorporates a new section on "Evolving Technologies," with general information on emerging technologies like cloud computing, zero trust architecture (ZTA), microservices, and artificial intelligence and machine learning (AI/ML).

On August 11, 2021, the FFIEC issued "Authentication and Access to Financial Institution Services and Systems," which replaced guidance issued previously in 2005 and 2011. The guidance provides financial institutions with examples of effective authentication and access risk management principles and practices for customers, employees, and third parties accessing digital banking services and information systems.[9]

In addition to the requirements around conducting risk assessments, implementing multi-factor authentication (MFA), and layered security, the latest guidance directs FIs to:

1

Establish the principle of **least privilege** while provisioning access and implement monitoring, activity logging, and reporting processes;

2

Ensure **secure credential** and application programming interface (API)-based authentication;

3

Establish **security controls** to secure email systems and internet browsers; and

4

Establish secure processes for customer call center and IT help desk operations and customer and user **identity verification**.

In its annual report, the Financial Stability Oversight Council (FSOC) includes cybersecurity as an area of vulnerability.[10] As the government broadly raises its assessment of the risk posed by FSI cyber incidents, firms should be thoughtful and intentional about their approaches to ongoing obligations under Regulation S-P and Regulation S-ID subpart C.

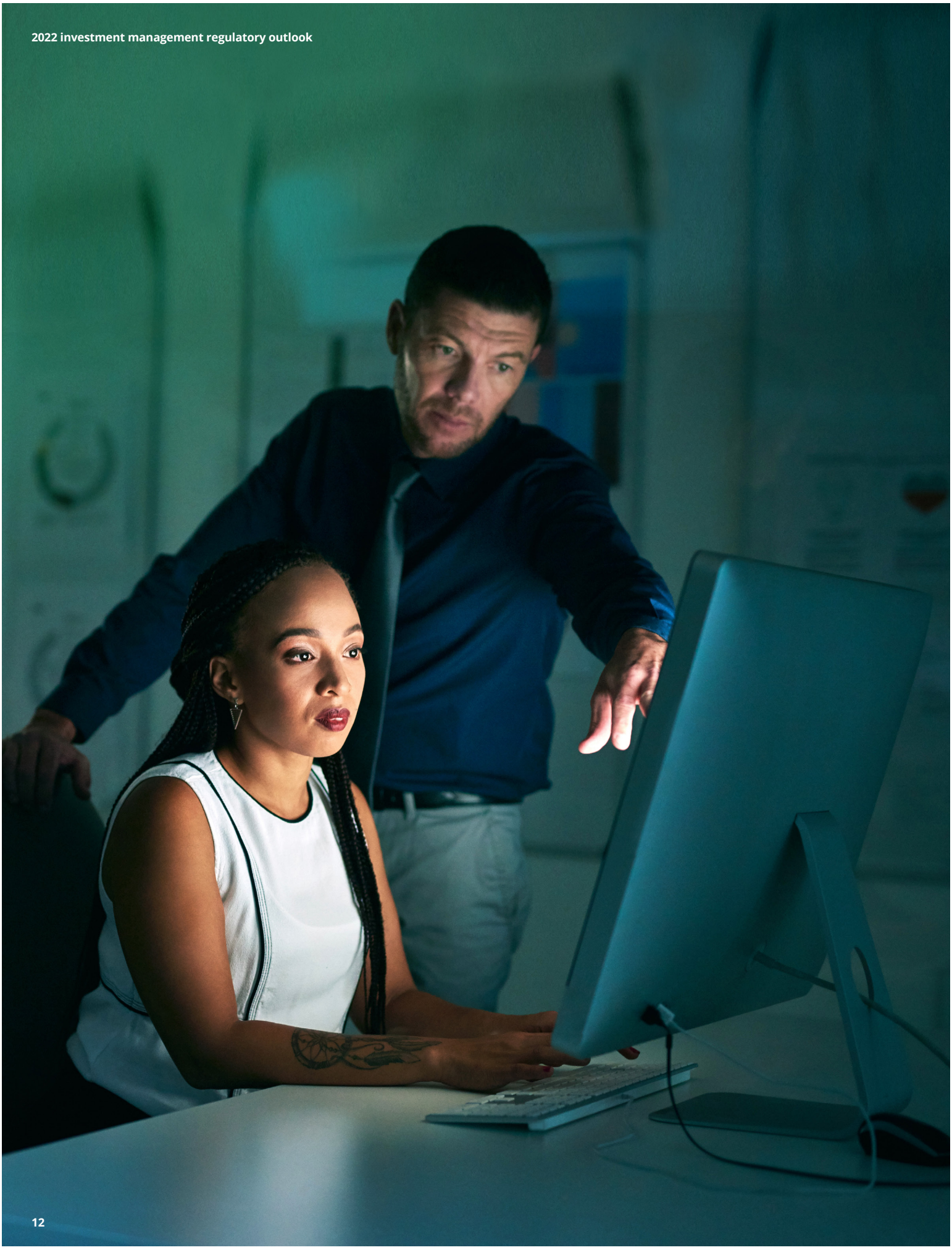
Changes to money market fund pricing

At the end of last year, the SEC proposed significant changes to its money market fund rules. The proposal: (1) increases liquidity requirements for funds, (2) prevents them from imposing liquidity fees or halting redemptions, (3) requires that institutional prime and institutional tax-exempt funds implement swing pricing, and (4) creates additional disclosure and record keeping requirements related to a negative interest rate scenario.

Implementing swing pricing would create operational complexities for firms and require capabilities to aggregate and analyze significant amounts of data within a short time period to implement. The SEC estimates that the liquidity requirements could result in as much as 15% of funds increasing their daily liquid assets and 50% increasing their weekly liquid assets, thereby increasing their demand for repos.[11]

Another important part of the proposed rule relates to how money market funds with stable net asset values (NAVs) might handle a negative interest rate environment. In this scenario, funds may need to convert to a floating share price, which would also result in operational complexities and likely necessitate coordination with service providers. The rule proposal would require funds to maintain records identifying the funds' intermediaries that have the capacity to adapt to non-stable share prices and those that do not.

The proposal increases barriers to entry and may limit the availability of these products, particularly institutional prime and institutional tax-exempt funds, and we expect the proposal to generate significant pushback from the industry.



Emerging regulatory topics

Digital assets

We expect federal regulators to use the full extent of their authority to regulate the crypto space in 2022. Currently, there are two key touchpoints between the federal government and digital assets: (1) regulated financial instruments (e.g., securities) and (2) regulated entities (e.g., banks and broker-dealers). In 2022, legislation might expand the scope of regulated instruments and entities. More likely, however, is that regulators will use their existing authorities to place requirements on firms and clarify their expectations for the crypto space.

The joint statement from the OCC, FDIC, and FRB—as well as a weighty interpretive letter from the OCC—signal to banks operating in the space that they should expect new obligations in conjunction with clarification of regulators' expectations. In particular, the statement from the OCC, FDIC, and FRB opens the door for 2022 issuances regarding balance sheet treatment, custody, facilitation of purchases and sales, collateralized loans, and stablecoins. Additionally, in 2022 we expect the SEC to further clarify its position on when a stablecoin is considered a security—potentially through continued enforcement actions.

We expect federal agencies to be very active in many areas during 2022, and the digital asset space will be no exception.

The fourth quarter of 2021 saw several weighty issuances that set the agenda for next year, including a report on stablecoins issued by the President's Working Group (PWG) and a joint statement from the Office of the Comptroller of the Currency (OCC), Federal Deposit Insurance Corporation (FDIC), and FRB regarding their plans to clarify banks' roles and requirements in this arena.

The PWG stablecoin report, issued in November 2021, lays out federal regulators' collective vision for the crypto space. The report calls on Congress to enact legislation that creates a cohesive federal framework for stablecoin regulation, including imposing bank-like prudential standards on stablecoin issuers and any entities that facilitate stablecoin arrangements. It also acknowledges that many stablecoins may in fact be securities (a frequent assertion of SEC Chair Gary Gensler) and recommends that federal regulators use existing authorities to control the space in lieu of congressional action. While legislative action is possible, other priorities may drive this year's congressional agenda, and gridlock is likely to take hold ahead of the midterm elections.

We expect federal agencies to be very active in many areas during 2022, and the digital asset space will be no exception. However, the legal classification of specific digital assets and services will ultimately determine the extent of regulatory authority in this area. Firms should be cognizant of the evolving definitions and ensure they are complying with relevant regulations, lest they find themselves targeted with regulatory action in 2022. The PWG stablecoin report should have the entire ecosystem on alert, with firms in the space closely monitoring the situation, planning for intensifying scrutiny, and proactively engaging with regulators.

Environmental, social, and governance (ESG) investing

Climate change and ESG issues remain top of mind for financial services regulators and industry groups, including those in the investment management space. Although there were relatively few rules proposed or finalized in 2021 specific to climate or ESG, there are indications that these areas will remain on regulatory agencies' agendas and that new rules may be introduced in the coming year.

In October 2021, the US Department of Labor (DOL)—in recognition of the fact that ESG factors may be material to the risk-return analysis of a portfolio—released a proposal under the Employee Retirement Income Security Act of 1974 (ERISA) clarifying that plan fiduciaries can consider climate change and other ESG factors when making investment decisions and exercising shareholder rights, including voting on shareholder resolutions and board nominations.[12] If finalized, the DOL rule could remove for ERISA plans certain barriers to selecting ESG investments so long as those selections are otherwise consistent with a prudent and loyal investment decision process. Comments on the proposal were due at the end of 2021 and a final rule is expected in 2022.

While the SEC did not introduce any climate- or ESG-specific rules in 2021, it did enhance its focus on climate- and ESG-related activities in firm examinations, including proxy voting practices and the practices of firms with products marketed as "green" or otherwise climate- or ESG-oriented. Looking ahead to 2022, it is generally expected that the SEC will release a proposal that addresses investment products that are marketed as green or considering ESG factors.

Preparing for 2022

The lack of extensive regulation around climate and ESG investing creates an opportunity for investment managers in 2022 to define the ESG investment process and its related education and marketing in 2022 and beyond.

For existing products that claim to use climate or ESG investing principles or criteria, firms might want to review the associated investment process (as well as the strategy description presented in offering documents, Forms ADV, marketing materials, etc.) with an eye toward creating a clearly defined procedure that examiners should find reasonable and appropriate. This review also could help investment managers uncover other portfolios in their lineup that are using ESG or climate filters but are not currently named or marketed as such, creating new marketing and branding opportunities.

Looking ahead to 2022, it is generally expected that the SEC will release a proposal that addresses investment products that are marketed as green or considering ESG factors.

Firms that use subadvisers might want to delve into their ESG and climate-focused investment processes to better understand their use of both qualitative and quantitative ESG and climate factors in selecting securities. As part of the process to define and describe its approach to ESG and climate investing, a firm might also want to take this opportunity to educate its shareholders, customers, board, and the public on how ESG metrics inform the overall investment process. Firms that proactively say what they do and do what they say on climate and ESG investing might be better positioned for potential ESG and climate regulations, exams, and inquiries in 2022 and beyond.

Emerging topics & valuation

Digital assets

While the issuance of SEC Rule 2a-5 is a leading topic in valuation for investment managers, it is by no means the only valuation topic worthy of attention in 2022. Two additional topics that have been gaining prominence recently and are expected to continue to be of interest are valuation questions raised by digital assets and sustainability/ESG investing.

Consistent with the requirements of Accounting Standards Codification ("ASC") 946, Investment Companies, digital assets should be recorded at their transaction price, which includes commissions and other charges that are part of the initial purchase.[13] The instruments are then subsequently marked to fair value.

The subsequent changes in fair value can represent challenges that investment companies will need to consider, particularly as they try to identify the principal or most advantageous market for the digital assets they hold. For example, many investment companies transact through brokers and the over-the-counter ("OTC") market and not directly through one of the numerous exchanges on which digital assets trade. The accounting guidance in ASC 820, Fair Value Measurement, states that the market in which a company transacts is presumed to be the principal market for that instrument.[14] However, pricing information may not be readily available from the OTC market, so some market participants then look to other sources, including the various exchanges and pricing aggregators for use as inputs in their valuation estimates of digital assets. Investment managers should consider whether the pricing information they obtain from those sources is reliable and representative of orderly transactions in an active market. Further, any adjustments made to those prices used as inputs should be considered and documented by the investment manager.

ESG Investing

ESG investing is another significant trend that has valuation implications. ESG, broadly speaking, leaves a lot of ground for investment managers to cover. Three areas, in particular, pose valuation challenges that the industry will continue to deal with in the coming years:

Company valuation. ESG raises a number of questions related to the valuation of companies. Many investors are clamoring for more disclosure and increased standardization to increase comparability amongst companies. Globally, regulators and various standard setters have responded with new or proposed guidance. Expect to see more action in this space in the coming years. As this space continues to grow and the investment community continues to adopt ESG-related strategies, we may see more evidence of the direct impact on the valuation of companies through divergences in the cost of capital for companies that are impacted by the application of these strategies and investor preferences.

Green bonds. Green bonds, issued by both corporate and sovereign issuers, have been a growing fixed income investment class for over a decade and come in many different flavors. The valuation of these instruments can be complex, depending on the structuring of the instrument, which may include securitization structures, indexed payments or tax advantages, among other features.

Traded products. In addition to green bonds, other ESG-related instruments are beginning to proliferate. Carbon offsets have traded in various jurisdictions globally for many years. In the United States, California, has established a cap-and-trade program that has attracted investor attention recently. As those markets grow, related markets, like derivatives and investment vehicles focused on such instruments, will undoubtedly grow as well; all representing different valuation questions that will need to be answered in the years ahead.

Diversity, equity, and financial inclusion in the investment management industry

The investment management industry continues to struggle with low levels of gender and racial diversity among investment professionals, boards, service providers, and minority-owned or female-owned investment firms. As reported by the SEC Asset Management Advisory Committee (AMAC), of the $70 trillion in assets under management (AUM) across the global financial universe, less than 1% is managed by minority-owned or women-owned firms. Also, percentages of ownership interest by women and underrepresented minorities in asset management firms is disproportionately low by any objective measure.[15]

Efforts to move the needle were accelerating before the pandemic; however, some measures of workplace gender equality seemed to have regressed.[16] Now, the need for improvement is greater than ever as pandemic challenges remain, and new ways of working introduce different risks to the recruitment, retention, and advancement of diverse talent.

Recent regulatory activity includes:

- The SEC announced plans to propose and **finalize new disclosures on board diversity** as part of its rulemaking agenda (June 2021).[19]
- The SEC's sub-committee on diversity and inclusion (under the AMAC) documented the need for **stringent mutual fund requirements on diversity** and board diversity disclosures related to racial and gender diversity (July 2021).[20]
- The SEC approved Nasdaq's proposal to set **baseline disclosure requirements** on board diversity and impose a comply or disclose requirement (August 2021).[21]
- New state rules such as SB 826 and AB 979 taking effect that **require minimum levels** of gender and race diversity respectively.[22]
- Various bills in Congress proposing **increased diversity on corporate boards** (e.g., H.R. 1277 Improving Corporate Governance Through Diversity Act of 2021).[23]

Financial inclusion is the process of providing financial services to unserved and underserved individuals and businesses in an affordable, sustainable, and ethical way.

Regulatory activity and scrutiny in this area is increasing, and Deloitte is seeing significant efforts to improve by asset management firms, boards, key service providers, and the companies in which mutual funds invest. Contributing factors include disclosure requirements and "comply or disclose,"[17] as well as the AMAC's recommendations and data showing broad investor and market interest in diversity disclosure by asset management firms.[18]

DEI efforts might fall short without a broader focus on financial inclusion. Financial inclusion is the process of providing financial services to unserved and underserved individuals and businesses in an affordable, sustainable, and ethical way. Examples include providing access to traditional credit through banking and insurance products; providing saving mechanisms for health care or education; and providing access to mutual funds and other investment products. The goal is to enable underserved customers and market segments to benefit from economic growth.

Investment advisers, fund distributors, and other service providers in the investment management sector should consider expanding their engagement with underinvested communities—increasing those communities' understanding, opportunities, and channels for participating in investment products and services. This can help boost economic opportunities among underserved and unserved markets and help people in those markets build wealth.

Having an established framework for financial inclusion can better position leaders to assess and address their organizations' financial inclusion strategy across multiple dimensions including:

- **Organization**[24], which covers how firms consider financial inclusion within their own workforce.
- **Offerings**[25], which considers how firms develop and deploy products and services to reach underserved and unserved communities.
- **Community**[26], which involves making commitments to the geographies and communities where the organization recruits, operates, and invests.
- **Ecosystem**[27], which helps enable firms to amplify their impact through vendors, partners, and public platforms.

This should help facilitate an organization's efforts to drive desired financial inclusion outcomes, and advisers and fund service providers can use the framework to evaluate the strategic, operational, and technological impacts on their stakeholders (i.e., workforce, customers, vendors, partners, and the external marketplace) across the dimensions.

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Looking ahead

The rulemaking process is very procedural, and the impacts of any major regulatory proposals to emerge in 2022 will not be felt overnight. Nevertheless, firms should remain alert and engage with policymakers while their efforts can have maximum impact (before the final rule stage). Since firms are likely to live with the rules that are proposed in 2022 for potentially years to come, it is well worth their effort to engage with the process early and often.

Similarly, firms must not lose sight of their ongoing and impending obligations. In conjunction with new rulemaking, we expect regulatory enforcement to be more vigorous than in recent years. Given the gravity of some of the areas under regulatory consideration, 2022 might frame the business and regulatory environment for financial services in the United States for the foreseeable future.

Endnotes

1. Additionally, in 2022 the SEC is contemplating improvements to market structure for the following: US Treasuries, equities, corporate bonds, municipal bonds, and digital assets. Any fundamental changes to these markets are likely to have downstream impacts on investment managers.
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16. Primarily, female workforce participation rates. For more information about firms' DEI practices, see Deloitte's Financial Inclusion survey: https://www2.deloitte.com/us/en/insights/industry/financial-services/alternative-data-innovation-financial-inclusion.html
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18. SEC, AMAC, "Recommendation of the Subcommittee on Diversity and Inclusion," July 7, 2021.
19. SEC, "SEC announces annual regulatory agenda," press release, June 11, 2021.
20. SEC, AMAC, "Recommendation of the Subcommittee on Diversity and Inclusion," July 7, 2021.
21. SEC "Order Approving Proposed Rule Changes, as Modified by Amendments No. 1, to Adopt Listing Rules Related to Board Diversity and to Offer Certain Listed Companies Access to a Complimentary Board Recruiting Service Release No. 34-92590," August 6, 2021.
22. Office of the California Secretary of State, "Diversity on Boards," accessed January 2022.
23. "Improving Corporate Governance Through Diversity Act of 2021," H.R. 1277, 117th Cong. (2021), introduced in House February 24, 2021.
24. Deloitte, "Driving purpose and profit through financial inclusion." March 30, 2021.
25. Ibid.
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27. Ibid.

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