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2025 investment management regulatory outlook

Center *for* Regulatory Strategy US

Message from the Deloitte Center for Regulatory Strategy

In 2025, the approach of regulators potentially could reverse course as the Trump administration embarks on its agenda. Former Securities and Exchange Commission (SEC) Chair Gary Gensler stepped down effective January 20, 2025, and President Trump has named former commissioner Paul Atkins as his nominee to lead the SEC.[1] In addition to changing priorities from a new chair, the pace of regulatory change affecting the investment management industry potentially could be slowed further by recent major court rulings.[2] As the pace of regulation abates and the SEC's priorities change, firms can take more strategic actions to position themselves for 2025 and beyond in response to these shifts.

For our *2025 investment management regulatory outlook*, we've placed regulatory initiatives on a continuum from immediate concern to regulation around the corner to areas of continued focus. In our view, there are five major regulatory themes for firms to consider.

- An unfinished agenda with policy reversals likely
- Blowback: The judicial and political brake on regulation
- Enforcement and rulemakings on the move
- Rules on the horizon and topics to watch
- Proposals that have stalled

Throughout this report, we provide our assessment of the regulatory and enforcement changes—and pressures—that may have the greatest impact on investment management firms in the coming year, with practical considerations to help you better position your institution for the challenges ahead.

We hope you find our outlook to be a helpful guide that will allow you to better understand how these regulatory changes and challenges in 2025 might have an impact on your institution. As always, we are here to help you chart the course.

Sincerely,

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An unfinished agenda with policy reversals likely

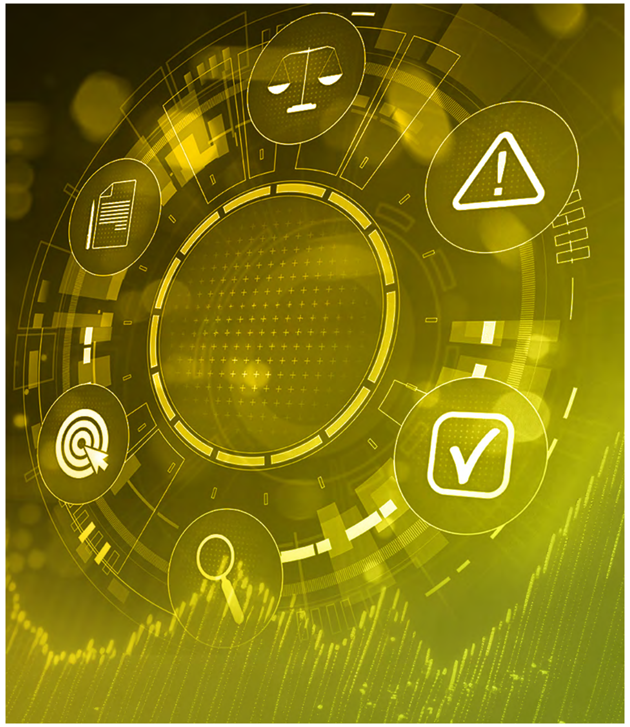
With the reelection of President Trump to a second, nonconsecutive term, financial regulatory policy is likely to reverse course for the second time in eight years. The outgoing administration leaves plenty of work for the industry to do, and the new administration needs time to embark on its agenda. Nevertheless, the change in control of Washington likely shifts the pendulum back to a deregulatory focus with plenty of implications for firms. As a candidate, Trump pledged his second administration "will eliminate a minimum of ten old regulations for every one new regulation," and has signed an executive order to that effect.[3]

Certain priorities of the previous SEC chair, such as a proposed safeguarding rule, likely will no longer move forward.[4] Other unfinished proposals, such as Safeguarding Advisory Client Assets;[5] Cybersecurity Risk Management for Investment Advisers, Registered Investment Companies, and Business Development Companies;[6] and Outsourcing by Investment Advisers,[7] likely will languish for the foreseeable future, offering some breathing room to firms complying with a range of regulatory items for the past several years.

Finalized items from Chair Gensler's agenda could be undone subject to the notice-and-comment requirements of the Administrative Procedure Act (APA).[8] Over the course of the next year, it will become more apparent which Biden administration initiatives the new Trump administration seeks to unwind.

The wheels of enforcement likely will continue to turn, at least until new appointees to lead agencies are in place to put on the brakes. President Trump's choice to lead the SEC is a former commissioner, cryptocurrency advocate, and "known for having a strong free-market bent" according to the Associated Press.[9] In the past, Atkins has opposed large fines for corporations, suggesting that they unduly punish shareholders.[10] We expect the that continued enforcement and related significant fines for electronic communications and records retention likely will cease. Any future enforcement priorities will likely be focused on investor protection and compliance with fiduciary standards. In addition, we expect the new regulatory climate to be more permissive with regard to scrutiny of mergers and acquisitions, particularly of cryptocurrency, private credit, and hedge funds; as well as toward new and novel products, such as exchange-traded fund (ETF) share class structures and retail alternatives.

Industry participants likely will have more flexibility to innovate and can expect rulemaking activity under the Trump administration to focus on streamlining firms' compliance requirements or otherwise lightening their regulatory burden at the federal level. Some states, however, may seek to layer on their own regulatory requirements if they perceive federal rules as becoming too lax.



Blowback: The judicial and political brake on regulation

The world after *Chevron, Jarkesy*

With 2024 rulings that address foundational elements of agency action and process, recent rulings by US courts have cast a shadow over agency interpretations and jurisdiction of certain enforcement actions.[11] Less deference likely will be given to actions overseen by regulatory agencies and undertaken through administrative processes. This shift indicates a potential reduction in the authority and influence of regulatory agencies.

The US Supreme Court decision negating the *Chevron* doctrine essentially means that judges—and not regulators—will have the final say on what is a reasonable interpretation of an ambiguous statute.[12] In the past, regulatory agencies had wide latitude in interpreting ambiguous statutes and the legislation that enabled their rulemaking. Now, courts may question the rationale of agency actions and interpretations. Where statutes are ambiguous, courts will now have the ability to use their independent judgment on agencies' authority to issue rulemaking, which could leave agencies with less power to issue rules in areas where Congress has not been explicit.

While the *Loper Bright* opinion limited retroactive application and, therefore, isn't expected to lead to the overturning of existing rules, it could have significant impact on agencies' rulemaking authority going forward.[13]

The *Jarkesy* ruling had a direct impact on the SEC as it often relies on administrative or in-house courts to levy penalties in certain cases.[14] In *Jaresky*, the US Supreme Court affirmed the right to trial by jury in securities fraud cases involving civil penalties. It involved a case brought by the SEC against a defendant in a civil matter seeking to levy a substantial fine, relying on a federal statute. Such logic applies in other SEC rules and enforcement actions. The *Jarkesy* ruling is expected to impact and potentially slow the pace of enforcement actions that depend on administrative courts in securities fraud cases.

The defeat of the Private Fund Adviser Rule

The US Fifth Circuit vacated the Private Fund Adviser Rule just one year after it was adopted—a significant setback for the SEC.[15] The rule comprised five separate categories, including a requirement that private fund managers provide investors with more detail about quarterly fees and expenses and a prohibition on firms giving some clients certain preferential terms, including preferential treatment to any "material economic terms," unless they satisfy certain specified exceptions. The US Fifth Circuit found that the SEC was beyond its authority in enacting the rule and treated all five sub-rules equally.[16]

The Court ruled that the SEC's reliance on Section 206(4) of the Advisers Act in the rule was "pre-textual" and that it failed to establish a rational relationship between the Private Fund Adviser Rule and how it would prevent fraud.[17] The SEC passed the deadline to appeal to the US Supreme Court.[18]

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Enforcement and rulemakings on the move

On October 21, 2024, the SEC's Division of Examinations released its 2025 examination priorities. The SEC has stated that this year's examinations will prioritize existing and emerging risk areas, such as fiduciary duty, cybersecurity, and artificial intelligence.[19] Under new SEC leadership, we expect enforcement focus areas to have a more direct line to investor protection, such as fiduciary obligations or the marketing rule. In our view, managing firms' response to these areas should be investment firms' highest priority.

Enforcement

Electronic communications and record retention

In the past year, the SEC, along with the Commodity Futures Trading Commission (CFTC), accelerated enforcement of rules regarding the monitoring and retention of electronic communications.[20] The first targets of enforcement were typically the broker-dealer arms of large banks, but subsequently RIAs were swept up in the SEC's enforcement efforts.

One critical conclusion from these enforcement actions is that the SEC is not only focused on off-channel communications; the agency is also concerned with the likelihood that firms without adequate records preservation could hinder the agency's ability to conduct effective supervision and, potentially, investigations of industry participants, since one investigation can uncover compliance failures at other institutions. Regulatory action is also moving from big institutions to smaller ones, including investment and wealth management firms, insurance companies, and credit agencies.[21]

In announcing fines, regulators have given clear guidance: If a firm discovers a compliance failure and takes significant steps to remediate and then self-reports the failure to the SEC, it may receive significantly reduced penalties.[22] Regulators have also recommended specific policies including permitting only trackable electronic channels for business communications and prohibiting the use, for business purposes, of any electronic channels that allow for anonymous or instant self-destruct communications. Firms are encouraged to establish and enforce specific policies for the business use of personal devices.

In response to the wave of enforcement actions, some institutions are outsourcing compliance monitoring of electronic communications, in addition to requiring third-party software on personal devices that enables archiving or forbidding the use of personal devices for business communications altogether. Institutions' compliance, legal, and technology teams are engaging with the business to understand their communication needs and implementing technologies and policies that both permit communication channels that meet business needs and enforce consistent and consequential discipline for off-channel communications.

In the new administration, however, we can expect sweeps for electronic communications violations and the attendant fines for such violations to abate. In addition, there is also the possibility that, under new leadership, the SEC would look to modernize recordkeeping rules for today's digital word.

Notwithstanding our view that electronic communications specific enforcement likely will abate, institutions should recognize that review of electronic communications will be an integral part of any examination; regardless, regulators see this as a central aspect of regulatory compliance, since evidence of communications is at the heart of providing the necessary documentation to substantiate actions, decisions, and adherence to regulatory requirements.

Marketing rule

Enforcement of this 2020 rule is focused on whether firms have established written policies and training to prevent violations.[23] The rule's recent revisions codified the responsibilities of RIAs whenever they are communicating to potential clients regarding securities and services, including on social media. The revisions also take aim at testimonials or endorsements and whether they are paid, whether in cash or some other form of compensation.[24] It also extends to third-party ratings and performance data that often appear on a RIA's website, which RIAs have long been required to substantiate.

Such content would therefore be subject to a review of whether the third-party rating is provided by a person or an entity that has no relationship to the RIA. RIAs would also need to apply other tests of a third-party rating and disclose these to the SEC.

This two-part process—due diligence and disclosure—will likely require new capabilities for many RIAs who are not used to such a requirement.

In our view, many firms are still struggling to meet the SEC's marketing expectations. Regulators are focused on untrue statements in advertisements, or the omission of key facts.[25] RIAs can consider conducting greater review of their direct and indirect marketing efforts, especially their websites and basic promotional materials. Such reviews should focus on any third-party ratings of their products or services to ensure that such ratings are accurate and follow a sound methodology and structure. Documentation of such methodology would be preserved. In addition, RIAs should be particularly focused on removing and avoiding any statements in public-facing materials that can't be supported or omitting key facts that would undermine the substance of any claim.

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Adherence to fiduciary standards of conduct

One of the SEC's 2025 exam priorities concerning RIAs pertains to the adherence of fiduciary standards.[26] Like the SEC's Reg BI, which aims to enhance investor protections and ensure that retail brokerage customers receive recommendations that are in their best interest,[27] the SEC's fiduciary standards profess a duty of care and loyalty to clients, making it clear that RIAs must always place client interests above their own and eliminate or disclose to clients all conflicts of interest, as appropriate.

Certain recommendations receive enhanced scrutiny given their fee structure, complexity, or volatility. These recommendations include: (1) high-cost products; (2) unconventional instruments; (3) illiquid and difficult-to-value assets; and (4) assets sensitive to higher interest rates or changing market conditions. RIAs should take a closer look at governing policies and procedures, especially around conflicts of interest, client recommendations, and account selection practices (e.g., brokerage versus advisory). The spotlight is on, and if only one thing is crystal clear, it is that regulators are sending a strong message to those offering advice and managing client money: Do the right thing, because we're watching you.[28]

Rulemaking

AML/CFT rules and programs: The Financial Crimes Enforcement Network (FinCEN) has published a final rule that requires certain investment advisers (IAs) to apply anti-money laundering (AML) and countering the financing of terrorism (CFT) requirements pursuant to the Bank Secrecy Act (BSA).[29] The final rule expands the definition of "financial institution" under the BSA and defines "covered IAs" as (1) IAs registered or required to register with the SEC (RIAs) and (2) IAs that report to the SEC as exempt reporting advisers (ERAs) pursuant to the Investment Advisers Act of 1940. IAs advising a mutual fund may exclude the mutual fund from the RIA's AML/CFT program since mutual funds are already subject to the BSA program. The rule does not apply to several categories of IAs.[30] The rule includes implementation of risk-based AML/CFT programs, reporting of suspicious activity to FinCEN, and fulfilling BSA recordkeeping requirements among other provisions.

Regulation S-P: On May 16, 2024, the SEC finalized amendments to Reg S-P—its customer information protection rule.[31] The amendments require institutions to adopt incident response programs and establish a notification requirement when data breaches or potential data breaches put customers at risk of harm. This is a critical change and will require firms to spend time updating their data management programs to comply.

Names Rule: The SEC adopted amendments to rule 35d-1 (the "Names Rule") on September 20, 2023. The amendments broaden the scope of funds that must comply with the rule's 80% investment policy, which requires 80% of assets to be invested in accordance with the fund's name, and establishes enhanced disclosure and reporting requirements. The final amendments set separate compliance dates for firms based on their size, with the first compliance date coming for large entities in December 2025. Some initial steps firms can take to prepare for the changes include evaluating the scope of impacted funds, understanding gaps in data sources, and determining revisions that may need to be made to certain ESG fund disclosures.[32]

Rules on the horizon and topics to watch

Significant proposals issued during Chair Gensler's tenure remain unfinished for multiple reasons, including the volume of initiatives undertaken, vocal industry pushback to the most sweeping proposals, the departure of the division director last spring, and—most recently and most significantly—the departure of the chair himself.[33] With the arrival of a new chair under another presidential administration, the fate of each proposal may be unknown, but certain initiatives are less likely to move forward than others, including proposed swing pricing for open-end funds and ESG disclosures for RIAs and RICs. Other outstanding proposals—such as cybersecurity and outsourcing—are likely to languish or be reproposed to incorporate industry feedback, prior to any adoption. Rule finalization, examinations, and enforcement may arrive for these eventually.

The horizon

Investment adviser and investment company cyber rule: An SEC proposal would establish a cybersecurity framework requiring both RIAs and RICs to adopt and disclose ongoing cybersecurity defenses, technologies, practices, and related risk management protocols.[34] In a related corporate cybersecurity rule, finalized in August 2023, the SEC laid out increased expectations for cybersecurity programs at public companies.[35] Accordingly, the SEC's goal isn't to prescribe specific tactics to reduce cybersecurity threats but rather to raise the overall level of cybersecurity readiness and responsiveness and help the investing public to better understand the cybersecurity defenses and policies of the firms they entrust with their funds.

Outsourcing by investment advisers: The SEC's proposed rule on outsourcing would establish an oversight framework for RIAs that outsource "covered functions," which are those that are necessary to provide advisory services in compliance with federal securities laws, and if not performed or performed negligently, would be reasonably likely to cause a material negative impact on clients or on RIAs' ability to provide investment advisory services.[36] The major components include due diligence requirements, periodic monitoring, and assessment; books and records requirements; third-party recordkeeping requirements; and new Form ADV requirements.

Topics to watch

Artificial Intelligence

Firms' use of AI (e.g., predictive analytics and Generative AI) has attracted regulatory attention.[37] Regulators are focused on whether firms understand how their analytics and AI-enabled tools work and the specific risks to which they are exposed; how large language models are trained; and whether these tools are transparent and available for examination.[38] They have identified many different sources of risk and potential abuse from the use of AI at financial institutions. Most critically, regulators are focused on whether AI could ignore or establish conflicts of interest, compromise customer privacy, or contain hidden sources of bias, and whether it can create systemic risk.[39] The new administration could change the focus to encourage adoption.[40] Nevertheless, AI should be handled as both a technological and governance challenge. Decision-makers will need to focus both on what AI can do as a technology and how AI needs to be managed as a potential source of risk.

For now, RIAs and others considering deploying AI-enabled solutions should be prepared for eventual rules, particularly at the state level, that would require certain governance and testing standards, written policies on AI use, and protections on the use of any personal and private data. As companies continue to adopt AI, it is essential to develop strong model risk management programs that extend beyond simple model risk inventories and governance procedures. This should involve comprehensive testing of AI tools to verify their reliability and accuracy. It may be difficult, as firms using and implementing AI-enabled tools are typically focused on applying them in automated investment tools, trading algorithms, and risk management.

Firms should establish a governance framework over any use of AI to include leaders with oversight of operations, technology, and compliance. In addition, firms should conduct a technology inventory so that it is known where AI and predictive analytics might be deployed in the business, whether in robo-advisors, chatbots, investment screens, or elsewhere. Testing AI models is another best practice to promote compliant outcomes. Since the rules on AI's use and governance are likely to evolve, firms should keep a close eye on both federal and state rules and procedures regularly subjecting themselves to internal reviews to identify emerging challenges. Finally, firms should make sure that any development or deployment of AI and predictive analytics are integrated into a conflict-of-interest management program and conduct regular assessments to see if conflicts may be evolving over time.

Sweep accounts: The SEC and the Financial Industry Regulatory Authority (FINRA) have previously issued warnings over the adequate compensation to investors for the value of their cash holdings when those sweep deposits are used to earn interest by loaning the funds.[41] What's more, there's the potential for RIAs to be accused of violating conflict-of-interest rules if they benefit from the sweeps through their relationships with banks. For now, the primary focus on sweep accounts is confined to civil litigation. Our view is that enforcement could be coming next.

Account takeover fraud: With a rise in account takeovers, RIAs should look to increasingly build their own cyber resiliency as well as policies and processes to respond even when account takeover fraud stems from a breach caused by a customer's failure to protect their own financial accounts.[42] Ideally, such policies and processes should enable the RIA to assess fault and the source of risk, limit and mitigate the fraud, address threats to other customers, and meet any AML and know-your-customer rules. Importantly, RIAs may need to disclose any cybercrime incidents.

Investment adviser oversight: FINRA is taking a harder line on the expectation that wealth managers oversee anyone who is working under their supervision as a broker or investment adviser representative of a dual-registered RIA.[43] FINRA has received approval from the SEC to treat private home offices of brokerage employees as "non-branch locations." This would, in effect, subject these locations to compliance reviews every three years (a traditional branch is inspected annually). Such home offices may not be used for client meetings, or handling client securities. FINRA also announced that it will allow firms to conduct compliance reviews of home offices remotely.

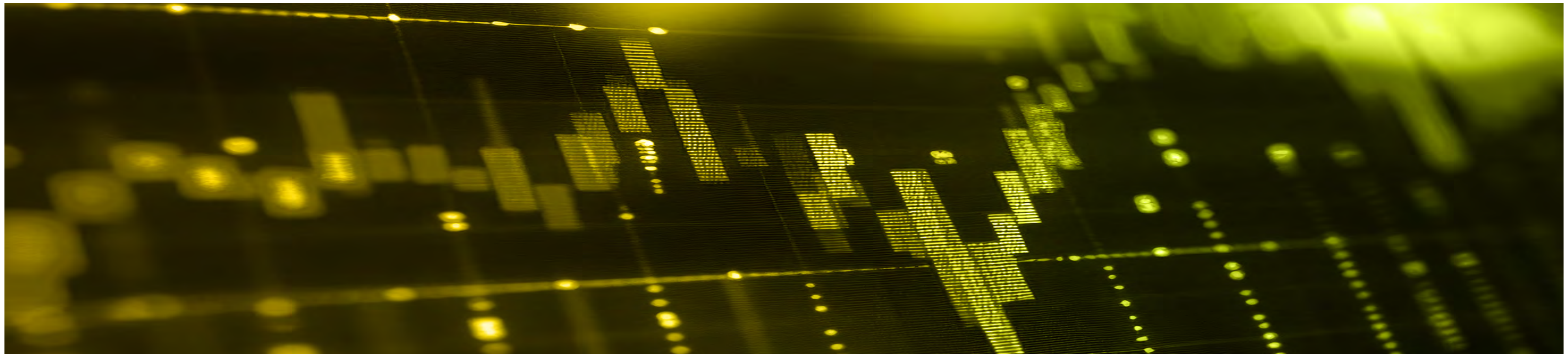
Proposals that have stalled

In our view, the rule proposals below likely are of less interest to the new administration:

Swing pricing for open-end funds: An SEC proposal to require swing pricing for open-end funds, which met fierce pushback from the industry, likely will be abandoned by incoming leadership. Even prior to the November 2024 election, the rulemaking appeared to be paused as the agency moved forward in August with amendments to reporting requirements on Forms N-PORT and N-CEN instead.[44] In effect, these reporting requirements will increase the frequency of disclosures to be shared by RICs with investors and regulators. Despite the moderated approach by the regulator, the SEC also may face judicial challenge on the Forms N-PORT and N-CEN amendments.[45]

Safeguarding rule: The SEC is currently progressing on a new safeguarding rule that would replace the existing custody rule. Under the proposal, RIAs would be required to have arrangements with qualified custodians for a broader variety of asset classes than exists currently, including crypto assets.[46] This proposal, published in February 2023 and subsequently opened for additional comments in August 2023, aims at giving retail investors more protection against the loss of their assets. Industry groups, including associations representing small and midsize RIAs, have voiced concerns about the costs and market effects of the rule.[47]

They argue that these new requirements may complicate custodial practices and add to their regulatory burden, potentially weakening the case for custody protections in certain situations. Similarly, banking regulators have also expressed concerns about the rule, saying it would undermine the case for custody banking.[48] The proposal remains under review, and the SEC has previously indicated this rule may be reproposed, allowing further industry feedback.



The road ahead

As a new administration takes the reins, regulatory headwinds are likely to continue to shift in the months ahead. With much of the existing SEC agenda for the investment management industry left unfinished, firms can potentially breathe a sigh of relief that the most onerous of proposals under consideration may have been avoided. Although the pace of new rulemaking may slow over the coming year, firms should remain vigilant in their preparations to meet upcoming regulatory mandates, such as the Investment Company Act "Names Rule."

As federal regulators pivot from a period of active rulemaking to likely more industry-friendly initiatives, firms will not want to be caught unaware by a potential uptick in mandates from certain states that may seek to fill a perceived void. The industry also has an important opportunity to have its voice heard by an administration with an open ear, and firms will want to be strategic about the priorities they choose to promote.

After several years of an assertive regulatory posture and lengthy agenda creating some uncertainty for firms, the industry should view the coming year as an opportunity to focus. 2025 should be a year of opportunity for firms prepared to seize the moment.

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30. IAs advising a mutual fund may exclude the mutual fund from the IAs' AML/CFT program. The final rule does not apply to IAs that register with the SEC solely because they are midsize advisers, multistate advisers, or pension consultants. The final rule also doesn't apply to IAs who are not required to report any assets under management (AUM) to the SEC, state-registered advisers, foreign private advisers, or family offices. For foreign-located IAs, the requirements are only applicable to (1) activities taking place in the United States and (2) advisory services to US persons or foreign-located private funds with US investors.

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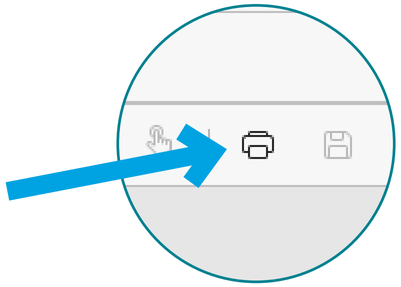

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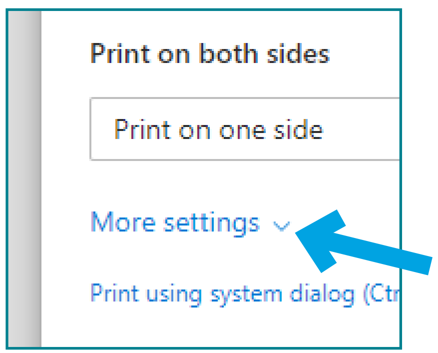
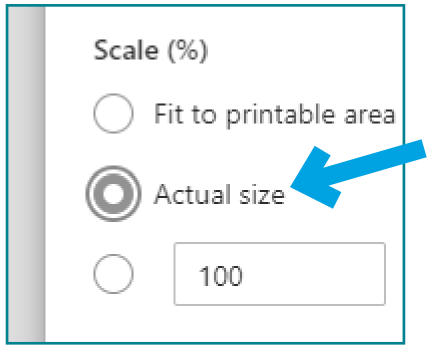
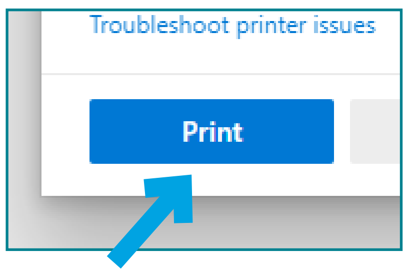


3. Change “Scale (%)” to “Actual size”

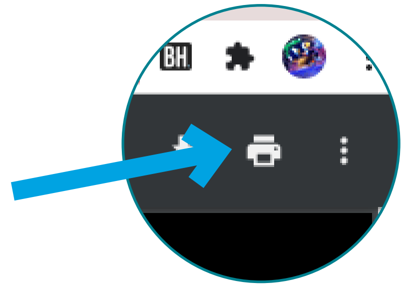


4. Click on the print button to print the document.

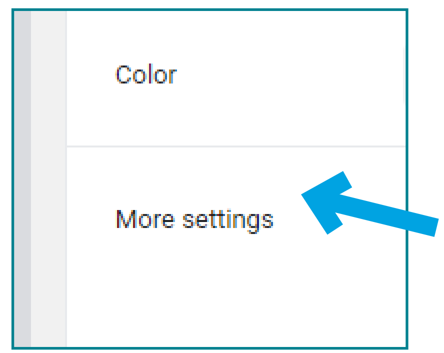


If printing from Google Chrome:

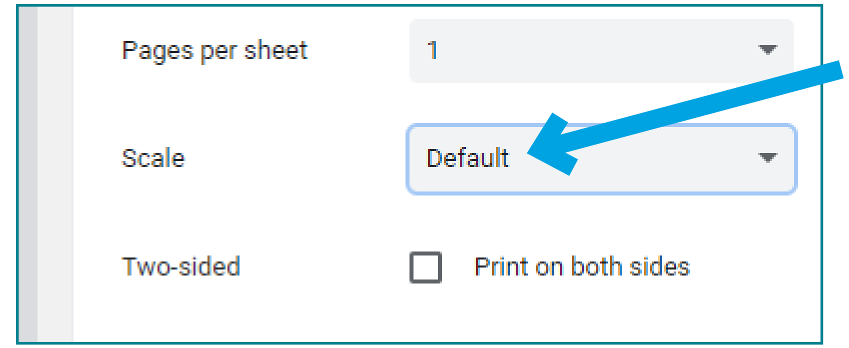
1. Click on the print icon



2. Scroll down to “more settings” and click to expand the menu



3. Change “Scale (%)” to “Default” (if needed)



4. Click on the print button to print the document.

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