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The Long and Winding Road: It's Time To Cross Once Again - K&L Gates

The SEC Proposes to Fix, Improve, and Modernize Mutual Fund Cross Trading Under Rule 17a-7

Introduction

At long last, the Securities and Exchange Commission (SEC) proposed amendments to Rule 17a-7 under the Investment Company Act of 1940 (1940 Act).¹ These amendments (the Proposed Amendments) would do many things, but most consequentially, the Proposed Amendments would fix the part of Rule 17a-7 that was broken with the adoption of the mutual fund valuation rule back in 2020: the effective exclusion of most fixed-income securities from the scope of Rule 17a-7.2

In addition, the Proposed Amendments would do the following:

- Allow cross trades at prices determined for net asset value (NAV) calculation purposes or current market prices based on unaffiliated pricing sources, including pricing vendors.
- Permit funds to make de minimis payments to unaffiliated parties for transaction-related operational services.
- Impose modernized oversight requirements, including pre-trade best-interest determinations, periodic pricing reviews, and annual reviews.
- Update associated recordkeeping and reporting requirements.

These Proposed Amendments are a welcome destination for the long and winding road that has been the regulation of cross trading by registered investment companies, but they would not deliver everything. Eligibility would remain tied to US generally accepted accounting principles (GAAP) valuation concepts, creating practical questions about how firms establish that a security qualifies when a trading opportunity arises. In addition, certain gaps remain. Illiquid investments whose valuations depend on significant unobservable inputs would still be excluded, and additional control affiliations would continue to block crosses between registered funds and many affiliated private funds. While the Proposed Amendments are certainly a win for the industry, these are issues that have been raised by the industry and will likely appear in the comment file. Comments are due by 14 December 2026.³

Ed. Note: For our purposes, this article states:

“If adopted, the SEC’s views would supersede inconsistent staff positions. The release identifies the United Municipal Bond Fund, Federated Municipal Funds, and Independent Directors Council letters, among others. Firms relying on those positions would need to assess how their programs fit within the amended framework.⁵⁵”

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