

# LSEG Pricing Service: SEC Rule 2a-5

On 3 December 2020, the US Securities and Exchange Commission (SEC) adopted rule 2a-5 (the rule) to modernise valuation practices across the mutual fund industry. The rule, which was adopted under the Investment Company Act of 1940, went into effect on 8 March 2021, with a compliance date of 8 September 2022. The rule seeks to provide a common fund valuation framework to be adopted by registered investment advisors and/or business development companies. It addresses valuation practices and the role of the board of directors (the Board), and provides requirements for determining fair value in good faith with respect to a fund's investments.

## Rule requirements

The rule requires the Board to be ultimately responsible for the valuation process. The Board may assign a designee (i.e., the investment advisor) to assess and manage the valuation process and material risks associated with fair value determinations; select, apply and test fair-value methodologies; and oversee and evaluate any pricing services used. With pricing vendors becoming an integral part of the fund valuation landscape, the rule addresses requirements related to pricing services such as performing the necessary due diligence, challenging prices, the use of appropriate methodologies, ensuring quality and a well-managed operation.



## Key highlights of rule 2a-5

The SEC framework includes the following actions that the investment firm must perform to determine the fair value of the fund's investments:

- **Valuation risk** – the SEC describes many risks that can materially impact valuations. Some of these include the types of investments being valued, use of unobservable inputs and risks that the pricing methodologies are inappropriate or not being applied consistently.
- **Fair-value methodologies** – selecting, testing and applying methodologies in a consistent manner as appropriate for determining the fair value. This requirement includes specifying the key inputs and assumptions specific to each asset class and the methodologies that will apply to new types of investments. Selecting and applying methodologies must be consistent and include calibration or backtesting.
- **Pricing service** – overseeing and evaluating any pricing services used. Processes for approving, monitoring and evaluating each service need to be established, as well as criteria for initiating price challenges. The following should be considered:
  - (i) the qualifications, experience, and history of the service
  - (ii) the valuation methods, inputs, and assumptions used for each security
  - (iii) the service's process for managing price challenges
- **Recordkeeping** – in addition to rule 2a-5 the SEC also adopted rule 31a-4, which requires funds or their advisers to maintain appropriate documentation to support fair value determinations for a period of six years. Board reporting on valuations is required quarterly, as is a thorough assessment of the valuation process – including pricing services – on an annual basis.

## Our offering

LSEG Pricing Service can support customers by providing them access to:

- Our service via existing client engagement support: this includes due diligence meetings, evaluation methodology walkthrough and deep-dive analysis meetings.
- Documentation including back-testing reports, methodology document, standard due diligence questionnaire FAQ, price challenge metrics and SOC 1 audit report.
- Transparency data through extractable data fields on Datascope Select.

## Accessing REPS

Customers can access our solutions via the following methods:

- Public website/toolkit at: [refinitiv.com/en/market-data/regulatoryservices/sec-rule-2a-5#solutions](https://refinitiv.com/en/market-data/regulatoryservices/sec-rule-2a-5#solutions)
- Extract data fields off Datascope Select (DSS)
- Schedule a call by sending an email request to: [REPS-Specialists@lseg.com](mailto:REPS-Specialists@lseg.com)

## FAQ

1. **What is your current offering for rule 2a-5?**  
Please refer to 'Our offering' section.
2. **Will you be changing your methodology once the 2a-5 rule is implemented?**  
Asset class methodologies will not change as a result of the rule.
3. **How do you currently test the quality and accuracy of your evaluated prices?**  
REPS has quality controls in place for each asset class which are tested by the SOC1 audit annually. Please refer to our SOC1 Type 2 audit report for a detailed description. In testing for accuracy, REPS compares its evaluated price to actual market transactions, (i.e., backtesting) where transactions are available.
4. **What kind of testing-related information will you provide to clients in response to the rule?**  
REPS will provide quarterly backtesting reports for certain asset classes such as Corporate bonds, Municipal securities, and Bank Loans.
5. **Do you have conflict-of-interest policy?**  
LSEG has a conflict-of-interest policy and an online training module that is mandatory for all staff.
6. **Do you have fourth-party risk oversight?**  
LSEG has a third-party risk management function that oversees vendors. As part of our internal controls, REPS performs annual due diligence of its key vendors with continuous monitoring.
7. **What is your price challenge process?**  
Clients can submit price challenges through either Datascope's Evaluation Connect or LSEG.com. Most challenges receive a response within 36 hours, but bulk challenges can take longer to resolve.
8. **Do you perform a deep-dive analysis of a security's price?**  
We perform deep-dive analyses by request and provide a formal report of the results.
9. **Other than those already discussed, do you anticipate making any other notable changes in response to the rule (e.g., to products, services, information or methods of communication)?**  
We are in the process of improving our data transparency for price input fields to be extracted via Datascope. We are also working on streamlining our deep-dive analysis process for a better customer experience.

