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Managing Your Blue Sky Resources in Three Easy Steps

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The question Boston Financial Blue Sky clients most frequently ask during their annual review is: *Is there anything further we can do to save on state Blue Sky fees?*

Management of Blue Sky has become a greater priority for many fund families because states are increasingly changing their Blue Sky statutes and regulations in an effort to raise revenue. Altering these filing fees is attractive to states because (a) Blue Sky requires self-reporting by fund families, rather than state management of fees and (b) since the National Securities Markets Improvement Act of 1996, there is comparatively less oversight necessary.

For example, in 2015, fee changes were enacted by Iowa and Alaska. Washington, notorious for having no annual cap on fees to notice file share classes, released an interpretive opinion in 2014 that clarified they do not offer an opportunity to cure when a share class sells in excess of its registered amount, and that triple penalty fees are due immediately. In 2009, Wisconsin drastically increased its fee range to notice file a single share class from $750 to $1,500 annually to $750 to $15,000 annually. These and other fee changes and policy interpretations can have a significant impact on all fund families.

While state fees are fixed, there are steps fund families can take to lower their Blue Sky reportable transactions, which in turn, can help rein in expenses.

Step 1: Maximize Exemptions: Almost every state has a "sales to existing shareholders" exemption in their securities act. This exemption is valuable in the 21 states that base fees on reported transaction activity. For oversight purposes it is easiest to establish and maintain the exemption in a single location. A best practice is to set up the exemption on your Blue Sky service provider's system. However, it can also be housed with your transfer agent or your brokers. Following initial implementation, you will want to review this exemption with the party where it is set up at least annually, and whenever you launch a new fund. The first step is to talk with your Blue Sky service provider about the best way to implement the exemption for your funds.

Step 2: Streamline Transaction Review: Step 2 is to establish policy and procedures for the review of Blue Sky transaction activity. These reviews can involve time consuming and costly interpretation of state statutes and regulations, potentially causing any monetary savings to disappear. Blue Sky transaction review policies and procedures can potentially save money for your firm.

One best practice option is to limit transaction reviews to those states that (a) base Blue Sky fees on reported transactions and (b) do not have a fee cap. At present, there are only five states that fit these criteria. In the states that do have fee caps, such as Louisiana and Montana, it is entirely possible that your Blue Sky provider could alert you to a multi-million dollar single transaction. But, because of fee caps, the associated state fee could be as low $50.00, making the transaction review more costly than the fee itself.

As an alternative to a policy of not reviewing Blue Sky transactions in states with an annual fee cap, consider informing your Blue Sky provider that you would like them to include the state fee associated with any transactions sent to you for review. This will allow for a case-by-case determination of whether or not reviewing the transaction is of any financial benefit.

Step 3: Define and Communicate What You Will Review: Your transaction review policy and procedures should spell out criteria that help your Blue Sky provider know what activity to send to your firm for review. Communicate these criteria to your provider, and plan to review them annually.

For example, one option is to inform your Blue Sky provider that you only want to be notified of transactions that cause a permit to exceed its registered amount. Assuming that your provider has rules in place that monitor permits to amend as needed based on transaction activity, this excess transaction rule may help ensure that only unusually large transactions are sent for review.

Another option, to be used alone or in conjunction with an excess transaction rule, is to tell your Blue Sky provider you want to review transaction activity when they suggest an amendment with a fee in excess of a certain dollar amount (e.g., $1,000 or $10,000), dependent on the typical activity of your funds.

Your Blue Sky provider can assist in determining a reasonable dollar amount by reviewing prior amendments. It is important to note that your Blue Sky provider should always be informing you of excess transactions on permits, particularly when penalty fees are involved, because frequent excess transactions could be a sign that a change is needed in your fund monitoring criteria.

Consistent implementation and clear communication are the keys to effectively managing Blue Sky fees. Make sure you and your Blue Sky provider are leveraging technology to maximize exemptions, and have clear rules about transaction review to reduce time spent on transaction activity that may not necessarily translate into savings for your firm.

Jennifer Kelefant is an Attorney, Blue Sky Administration for Boston Financial Data Services, Inc. Jennifer joined State Street's Blue Sky team in 2004, and moved to Boston Financial in 2013 when the business line was transitioned here. In her current role as consulting attorney dedicated to Blue Sky, Jennifer is the primary legal liaison for the Blue Sky team. Her responsibilities include contract review, monitoring state Blue Sky laws, reviewing legal updates to Blue Sky technology, working with state agencies overseeing Blue Sky registration, and assisting clients with exemption and registration matters. Jennifer was admitted to the Massachusetts Bar in 2010, and is a member of the State Regulation of Securities committee of the American Bar Association.