

February 3, 2016

CLIENT ALERT
SEC ANNOUNCES 2016 EXAM PRIORITIES

The SEC announced the 2016 examination priorities of its Office of Compliance Inspections and Examinations (“OCIE”).¹ The examination priorities reflect the practices and products that OCIE believes presents “potentially heightened risk to investors and/or the integrity of the U.S. capital markets,” and focus on the same three thematic areas as 2015:

1. Examining matters of importance to retail investors, including investors saving for retirement;
2. Assessing issues related to market-wide risks; and
3. Using evolving ability to analyze data to identify and examine registrants that may be engaged in illegal activity.

I. Examination Priorities

1. Examining Matters Important to Retail Investors

Retail investors have many choices when determining how to invest their money. In addition, the financial services industry provides a broad array of information, advice, products and services to retail investors to help them plan for retirement. The following

¹ A copy OCIE’s examination priorities for 2016 is available at <https://www.sec.gov/about/offices/ocie/national-examination-program-priorities-2016.pdf>

examination initiatives are designed to assess risks to retail investors that could arise from these trends:

- ReTIRE. OCIE will continue the multi-year examination initiative launched in June 2015 that focuses on the services SEC-registered investment advisers and broker-dealers offer to investors with retirement accounts. In this connection, OCIE will examine the reasonable basis for recommendations, conflicts of interest, supervision and compliance controls, and marketing and disclosure practices.
- Exchange Traded Funds (“ETFs”). OCIE will examine ETFs for compliance with applicable exemptive relief, unit creation and redemption. OCIE also will focus on sales strategies, trading practices, and disclosures involving ETFs, including excessive portfolio concentration, primary and secondary market trading risks, adequacy of risk disclosure, and suitability.
- Branch Offices. OCIE will review supervision of registered representatives and investment adviser representatives in branch offices of SEC-registered investment advisers and broker-dealers.
- Fee Selection and Reverse Churning. OCIE will examine investment advisers and dually-registered investment adviser/broker-dealers that offer retail investors a variety of fee arrangements. OCIE will focus on recommendations of account types and whether the recommendations are in the best interests of retail investors.
- Variable Annuities. OCIE will assess the suitability of sales of variable annuities to investors, as well as the adequacy of disclosure and the supervision of such sales.
- Public Pension Advisers. OCIE will examine advisers to municipalities and other government entities, and will focus on pay-to-play and certain other key risk areas related to advisers to public pensions.

2. **Assessing Market-Wide Risks**

To support the SEC’s mission to maintain fair, orderly and efficient markets, OCIE will examine for structural risks and trends, including focusing on the following initiatives:

- Cybersecurity. OCIE will advance its efforts in connection with its second initiative launched in September 2015, to examine broker-dealers’ and investment advisers’ cybersecurity compliance and controls.

- Regulation Systems Compliance and Integrity (“SCI”). OCIE will examine SCI entities to evaluate whether they have established, maintained, and enforced written policies and procedures reasonably designed to ensure the capacity and security of their SCI systems.
- Liquidity Controls. OCIE will examine advisers to mutual funds, ETFs, private funds that have exposure to potentially illiquid fixed income securities, and registered broker-dealers that have become new or expanding liquidity providers in the marketplace.
- Clearing Agencies. OCIE will conduct annual examinations of certain “systematically important” clearing agencies. Areas for review will be determined through a risk-based approach.

3. Using Data Analytics to Identify Illegal Activity

OCIE’s examination program is risk-based. In striving to detect risk, OCIE utilizes data from its own examinations and from regulatory filings to identify registrants with elevated risk profiles. Examinations initiatives that leverage these analytics include:

- Recidivist Representatives and their Employers. OCIE will use its analytic capabilities to identify individuals with a track record of misconduct and examine the firms that employ them.
- Anti-Money Laundering (“AML”). OCIE will examine broker-dealers’ AML programs, focusing on firms that have not filed the number of suspicious activity reports (“SARs”) that would be consistent with their business models. OCIE also will continue to assess broker-dealers’ AML programs, with an emphasis on the adequacy of the independent testing obligation, and the extent to which firms adapt their programs to current money laundering and terrorist financing risks.
- Microcap Fraud. OCIE will examine the operations of broker-dealers and transfer agents for activities that indicate they may be engaged in, or aiding and abetting, pump-and-dump schemes or market manipulation. OCIE also will assess whether broker-dealers are publishing appropriate quotes for or trading securities in the over-the-counter markets.
- Excessive Trading. OCIE will analyze data to identify and examine firms that are engaged in excessive or inappropriate trading.

- Product Promotion. OCIE will focus on detecting the promotion of new, complex and high risk products and related sales practices that give rise to suitability issues and breaches of fiduciary obligations.

II. Other Initiatives

In addition to the foregoing, OCIE expects to allocate examination resources to other priorities, including: municipal advisors, private placements (including review of offerings involving Regulation D of the Securities Act of 1933 or the Immigrant Investor Program (“EB-5 Program”)), never-before-examined investment advisers and investment companies, private fund advisers (maintaining a focus on fees and expenses and evaluating, among other things, the controls and disclosure associated with side-by-side management of performance-based and purely asset-based fee accounts), and transfer agents.

III. Conclusion

This description of OCIE’s examination priorities is not exhaustive, but does provide insight into the anticipated focus of examinations throughout 2016. In addition to the priorities described above, OCIE also will conduct examinations focused on “risks, issues, and policy matters that arise from market development, new information learned from examinations or other sources, including types, complaints, and referrals, and coordination with other regulators.”

You should assess your risks, especially in the areas that OCIE has designated priorities. Please call Meryl Wiener, any member of the corporate department listed below or your regulator Warshaw Burstein attorney if you have any questions concerning your risk profile or if you would like our assistance in helping you assess your risk profile.

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