



Exam Priorities for 2015

The Office of Compliance Inspections and Examinations (OCIE) of the Securities and Exchange Commission (SEC or Commission) announced their exam priorities for 2015. While this list is not exhaustive, it focuses on the areas the OCIE believes to be at highest risk.

The exam priorities were decided upon in consultation with the five Commissioners, senior staff from the SEC's eleven regional offices, the SEC's policy-making and enforcement divisions, the SEC's Investor Advocate, and the SEC's fellow regulators.

The 2015 priorities focus on issues involving investment advisers, broker-dealers, and transfer agents in the following thematic areas:

1. Protecting Retail Investors and Investors Saving for Retirement
2. Assessing Market-wide Risks
3. Using Data Analytics to Identify Signals of Potential Illegal Activity

Protecting Retail Investors and Investors Saving for Retirement

Products and services that were once only available to institutional investors are now being made available to retail investors. With this trend and the risks associated with offering sophisticated investment vehicles to retail investors, the OCIE is planning the following various examination initiatives:

- **Fee Selection and Reverse Churning** – Where an adviser offers a variety of fee arrangements, recommendations for accounts types will be reviewed to determine if they are in the best interest of the investor. Fees charged, services provided, and disclosures will also be reviewed.
- **Sales Practices** – Sales practices will be reviewed to determine if improper or misleading practices were used when recommending the movement of retirement assets from employer sponsored defined contribution plans into other investment accounts especially if they charge higher fees or impose greater risk.
- **Suitability** – Recommendations and determinations of complex investments will be evaluated to ensure due diligence was conducted, disclosures were made, and proper suitability was assessed.
- **Branch Offices** – The supervision practices of registered representatives' branch offices will be reviewed to identify any branches that are not adhering to the home office's compliance practices.

- **“Alternative” Investment Companies** – Funds offering alternative investment strategies will be assessed with a particular focus on (1) leverage, liquidity, and valuation practices and policies; (2) factors relevant to the adequacy of the funds’ internal controls including staffing, funding, and the empowerment of the boards, compliance personnel, and back offices; and (3) the method in which funds are marketed to investors.
- **Fixed Income Companies** – Mutual funds with significant exposure to interest rate increases will be reviewed to ensure compliance policies and procedures are implemented and investment and trading controls sufficient enough to ensure that their disclosures are not misleading and that their investment and liquidity profiles are consistent with those disclosures.

Assessing Market-wide Risks

The SEC’s mission includes investor protection, capital formation, and maintaining fair, orderly, and efficient markets. The OCIE will be examining structural risks and trends that may involve multiple firms or entire industries through the following initiatives:

- **Large Firm Monitoring** – The largest US broker-dealers and asset managers will be monitored to assess risks at individual firms and maintain early awareness of developments industry-wide.
- **Clearing Agencies** – Annual exams of all clearing agencies designated as systematically important, pursuant to the requirements of the Dodd-Frank act, will continue to be conducted.
- **Cybersecurity** – Broker-dealers and investment advisers’ cybersecurity compliance and controls will continue to be examined. Efforts will be expanded to transfer agents.
- **Potential Equity Order Routing Conflicts** – The OCIE will assess whether firms that are prioritizing trading venues based on payments or credits for order flow conflict with their best execution duties.

Using Data Analytics to Identify Signals of Potential Illegal Activity

The OCIE has made significant enhancements enabling them to efficiently and effectively analyze data. Using data analytics, they will focus on firms that appear to potentially be engaged in fraudulent or other illegal activities.

- **Recidivist Representatives** – Using analytics, the OCIE will continue to identify individuals with a history of misconduct and exam the firms that employ them.
- **Microcap Fraud** – Operations of broker-dealers and transfer agents will be reviewed for any activities that indicate they may be engaged in, or helping, pump-and-dump schemes or market manipulation.
- **Excessive Trading** – Data from clearing brokers will be analyzed to identify and examine introducing brokers and registered representatives that appear to be engaged in excessive trading.
- **Anti-money Laundering (AML)** – Clearing and introducing broker-dealers’ AML programs will be examined with a focus on firms that have not filed suspicious activity reports (SARs) or have filed incomplete reports or late SARs. For broker-dealers that allow customers to deposit and withdraw cash and/or provide customers with direct access to markets from higher-risk jurisdictions, their AML programs will be examined.

Other Initiatives

In addition to the main themes described above, the OCIE will allocate resources for other priorities including:

- **Municipal Advisors** – Newly registered municipal advisors' compliance with recently adopted SEC and MSRB rules will be assessed.
- **Proxy Services** – Select proxy advisory service firms will be examined to see how they make recommendations on proxy voting and how they disclose and mitigate potential conflicts of interest. Investment advisers' compliance with their fiduciary duty in voting proxies on behalf of investors will also be examined.
- **Never-before-examined Investment Companies** – Focused, risk-based exams of selected registered investment companies that have not yet been examined will be conducted.
- **Fees and Expenses in Private Equity** – Exams of private equity funds with regard to fees and expenses will be performed due to the high rate of deficiencies among advisers.
- **Transfer Agents** – Resources will be allocated to examine transfer agents, particularly those that are involved with microcap securities and private offerings.