

FINANCIAL SERVICES TRENDS

SEC OFFICE OF COMPLIANCE INSPECTIONS AND EXAMINATIONS: 2019 EXAMINATION PRIORITIES

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On December 20, 2018, the Securities and Exchange Commission's ("SEC") Office of Compliance Inspections and Examinations ("OCIE") issued its 2019 Examination Priorities Report (the "Report").

The OCIE's responsibilities include overseeing broker dealers, investment advisers, municipal advisors, mutual funds, the Financial Industry Regulatory Authority ("FINRA"), the Securities Investor Protection Corporation ("SIPC"), the Municipal Securities Rulemaking Board ("MSRB"), the Public Accounting Oversight Board ("PCAOB"), clearing agencies, and exchanges. Both investment advisers and broker dealers continue to be a major focus of the OCIE with approximately 300 of the 3,800 broker dealers, and approximately 2,200 of the 13,200 investment advisers being examined during fiscal year 2018. It should be noted that examinations by the OCIE have increased by 10% over fiscal year 2017.

The Report gives investment advisers and broker dealers insight into the examination priorities in 2019, with the understanding that the OCIE continues to focus on investor protection (especially retail investors). The Report also clearly states that the OCIE will continue to examine investment advisers that have not been examined in the past or have not been recently examined.

The Report lists themes of priority, which are of interest to both broker dealers and investment advisers:

- Matters of importance to retail investors (seniors and those saving for retirement)
- Compliance and risk in registrants responsible for critical infrastructure
- Select areas and programs of FINRA and the MSRB
- Digital assets
- Cybersecurity
- Anti-Money Laundering

Retail Investor Concerns

The Report devotes significant space to the area of retail investors, including noting the SEC's intention to prioritize:

- Review of fees charged in advisory accounts, in order to assess whether the fees charged are in accordance with client agreements. Firms should also note that the OCIE will focus on the adequacy

of disclosures surrounding fees, affiliated service providers, and other conflicts of interest.

- Appropriateness of investment recommendations (particularly to seniors), and the related supervision and oversight by firms to mitigate risks.
- Mutual funds and ETFs that track custom indexes, funds managed by newer advisors, and the oversight of the boards of these vehicles.
- Potential manipulation in sales of microcap securities by broker dealers, and sales practices related to those securities.
- Broker dealer compliance with SEC Rule 15c3-3 (the Customer Protection Rule), including procedures and controls.

Concerns Regarding Registrants Responsible for Critical Market Infrastructure

The OCIE will conduct annual examinations of clearing agencies that have been deemed systemically important (under Dodd-Frank), as well as examinations of other registered clearing agencies, transfer agents, national securities exchanges, and entities under Regulation SCI¹.

As always, it will be critical for entities that are responsible for critical market infrastructure to demonstrate their compliance with regulatory requirements, and how they have taken steps (on a timely basis) to correct deficiencies identified in prior examinations.

FINRA and MSRB

The OCIE will continue to examine FINRA and MSRB to review (a) the operations and regulatory programs, (b) the quality of the examinations of broker-dealers, (c) effectiveness of policies, procedures, and controls.

Digital Assets

With the rapid rise of the digital assets and digital asset market participants, this will be a key focus area for the OCIE. The focus will be on portfolio management of digital assets, trading, custody and safekeeping of client funds and assets, pricing, and controls. In addition, the OCIE will monitor the offer and sale of digital assets where they could be deemed to be securities.

¹ Per the SEC, Regulation SCI (Systems Compliance and Integrity) applies primarily to the systems of SCI entities that directly support any one of six key securities market functions - trading, clearance

and settlement, order routing, market data, market regulation, and market surveillance ("SCI Systems").



Cybersecurity

Cybersecurity continues to be a key priority for the OCIE especially related to information security and data loss prevention, policies and procedures (including training and incident response), access rights, and vendor management. Firms should continually assess their cybersecurity awareness and response, especially when there are changes in the environment (such as mergers, multiple locations, remote working environments, etc.).

Anti-Money Laundering (“AML”)

The Report also discusses the OCIE’s focus on the implementation of AML programs at broker dealers, including the independent testing.

For questions on this article (including assistance with digital assets, cybersecurity, or AML programs), please contact the team of seasoned professionals at Mazars USA.

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