

Alert | Financial Regulatory & Compliance



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SEC Announces 2023 Examination Priorities

On Feb. 7, 2023, the Securities and Exchange Commission (SEC)'s Division of Examinations (Division) announced its 2023 examination priorities (Exam Priorities). The **announcement** focuses on six different categories:

1. New Investment Adviser and Investment Company Rules
2. Registered Investment Advisers (RIAs) to Private Funds
3. Retail Investors and Working Families
4. Environmental, Social, and Governance (ESG)
5. Information Security and Operational Resiliency
6. Emerging Technologies and Crypto-Assets

This GT Alert discusses the Exam Priorities related to each of these categories.

1. New Investment Adviser and Investment Company Rules

The Division will focus on the new Marketing Rule (Advisers Act Rule 206(4)-1). Specifically, Division staff will assess whether advisers have:

- a. adopted and implemented written policies and procedures that are reasonably designed to prevent violations of the new rule by the advisers and their supervised persons; and
- b. complied with the substantive requirements of the new rule, including the requirement to have a reasonable basis for believing an adviser will be able to substantiate material statements of fact and requirements for performance advertising, testimonials, endorsements, and third-party ratings.

Additionally, the Division will focus on new rules applicable to investment companies, including the Derivatives Rule (Investment Company Act Rule 18f-4) and Fair Valuation Rule (Investment Company Act Rule 2a-5).

2. RIAs to Private Funds

The Division will review issues under the Advisers Act, including an adviser's fiduciary duty, and will assess risks, including a focus on compliance programs, calculation and allocation fees and expenses (e.g., post-commitment period management fees and valuation practices), advertising (under the new Marketing Rule), conflicts of interest, the use of alternative data, and Custody Rule compliance (e.g., timely delivery of audited financials and selection of permissible auditors disclosed in Form ADV.) The Division will also review private fund advisers' portfolio strategies, risk management, and investment recommendations and allocations, specifically focusing on conflicts and disclosures around these areas. In addition, the Division will focus on RIAs to private funds with specific risk characteristics, including highly leveraged private funds and private funds managed side-by-side with business development companies.

3. Retail Investors and Working Families

The Division will continue to address standards of conduct issues for broker-dealers and RIAs to ensure that retail investors and working families receive recommendations and advice in their best interests. Specifically, these examinations will focus on how registrants are satisfying their obligations under Regulation Best Interest and the Advisers Act fiduciary standard to act in the best interests of retail investors and not to place their own interests ahead of retail investor interests. Examinations will include assessments of practices regarding review of investment alternatives, management of conflicts of interest, and consideration of investment goals and account characteristics.

4. Environmental, Social, and Governance (ESG)

The Division will continue to focus on ESG-related advisory services and fund offerings, including whether funds are operating consistently with their disclosures. Additionally, the Division will evaluate whether ESG products are appropriately labeled and whether recommendations of ESG products to retail investors are made in the investors' best interests.

5. Information Security and Operational Resiliency

The Division will review registrant practices to prevent interruptions to mission-critical services and practices to protect investor information, records, and assets. In addition, exams of broker-dealers and RIAs will focus on the cybersecurity issues associated with the use of third-party vendors, including registrant visibility into the security and integrity of third-party products and services and whether there has been an unauthorized use of third-party providers.

6. Emerging Technologies and Crypto-Assets

The Division will conduct examinations of broker-dealers and RIAs using emerging financial technologies or employing new practices, including technological and online solutions to meet the demands of compliance and marketing and to service investor accounts. Examinations of registrants will focus on the offer, sale, recommendation of, or advice regarding trading in crypto or crypto-related assets and include whether the firm:

- a. met and followed their respective standards of care when making recommendations, referrals, or providing investment advice; and
- b. routinely reviewed, updated, and enhanced their compliance, disclosure, and risk management practices.

Conclusion

Firms registered with the SEC should be aware that the Exam Priorities list is not exhaustive, and exams may cover many issues not stated in this list. However, the Exam Priorities align with recent SEC announcements and activity. Accordingly, registered firms should take note of these priorities when reviewing compliance programs to ensure their compliance programs address the Division's focus if such priorities relate to their programs and practices. Further, examination findings can lead to enforcement referrals and, eventually, enforcement actions. As a result, firms should pay close attention to the Exam Priorities, as they may signal future enforcement priorities in the form of sweeps and other actions.

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