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SEC Staff Announces 2017 OCIE Examination Priorities

January 18, 2017

On January 12, 2017, the staff of the Office of Compliance Inspections and Examinations (OCIE) of the Securities and Exchange Commission (SEC) released its annual announcement on examination priorities in the coming calendar year. The 2017 examination priorities are organized around three thematic areas: (i) examining matters of importance to retail investors; (ii) focusing on risks specific to elderly and retiring investors; and (iii) assessing market-wide risks. As we have reported on previously, OCIE incorporates data analytics into the vast majority of its examination initiatives to identify industry practices and/or registrants that appear to have elevated risk profiles.

Advisers should note that on October 11, 2016, the SEC announced a record number of investment adviser enforcement cases for the agency's fiscal year 2016, which ended on September 30, 2016. Accordingly, advisers can expect that the SEC will lean heavily on OCIE as a resource for maintaining similar statistics for fiscal year 2017. While the 2017 announcement contains broad and general descriptions of areas on which the staff intends to focus, there are several key points to which advisers to hedge funds, private equity funds and other private funds should pay close attention.

Conflicts of Interest and Disclosure

Specific to private fund advisers, the announcement expressly affirms the staff's continuing attention to conflicts of interest and disclosure of conflicts as well as actions that create the appearance of benefitting an adviser at the expense of fund investors. In 2016, the SEC secured settlements with several private fund advisers in areas involving (i) charging portfolio companies operating partner oversight fees, and acquiring defaulting limited partner interests, without adequate pre-capital-commitment disclosure, (ii) the disclosure of accelerated monitoring fees, and (iii) the disclosure of how management fee offset provisions were calculated. In the days preceding the 2017 announcement, the SEC announced a settlement with a private equity fund adviser involving the alleged failure to disclose conflicts of interest arising from the adviser's principals' personal investments, board positions and familial relationships with several funds' due diligence providers. In articulating its focus in this area, the staff appears to indicate that there remain conflicts of interest and commensurate disclosure practices which it seeks to review and influence through its examination (and potentially enforcement) programs.

Pension Plan Advisers

The staff also references its interest in reviewing advisers to pension plans of states, municipalities, and other government entities. The announcement specifically noted that OCIE will assess how these advisers are both managing conflicts of interest and fulfilling their fiduciary duties. OCIE also will review other risks specific to these advisers, including potential pay-to-play arrangements and undisclosed gifts and entertainment practices.

Cybersecurity

As in the 2016 announcement, the staff also indicated that it will continue to focus on the area of cybersecurity in 2017. Specifically the staff will be evaluating cybersecurity compliance procedures and controls, including testing the implementation of those procedures and controls.

Other Areas of Focus

As a continuation from 2016, the 2017 announcement reiterates a focus on both never-before examined investment advisers and advisers employing individuals with what the announcement describes as a "track record of misconduct," whom the SEC refers to as recidivists. On September 12, 2016, OCIE had published a National Examination Program Risk Alert, which announced the staff's intention to focus on these advisers and, specifically, registered advisers' compliance programs and the supervision of advisory personnel that may pose an increased risk to advisory clients based upon prior infractions.

Whistleblowers and Other Tips

The SEC concluded its 2017 announcement by highlighting its receipt of tips, complaints, and referrals as a source of information guiding its examination program. The announcement also provides a hyperlink to the agency's webpage describing the process for reporting suspected misconduct to the SEC staff. As we highlighted previously, advisers should review the October 24, 2016 risk alert published by OCIE, which announced that the SEC exam staff intends to examine registrants' compliance with the Dodd-Frank Act's whistleblower provisions, as well as SEC enforcement activity in this area.

In conclusion, the staff's 2017 announcement sets forth a basic roadmap registrants subject to SEC oversight can expect the agency to follow. While the announcement itself covers all entities regulated by the SEC, advisers to private funds would be well-served to devote time and resources to assessing and assuring their preparedness in the specific areas articulated above.

Related Professionals

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