

SEC 2013 Examination Priorities

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The Securities and Exchange Commission's National Examination Program (NEP) published its examination priorities for 2013. The examination priorities address market-wide issues as well as issues with respect to the following program areas: (i) investment advisers and investment companies, (ii) broker-dealers, (iii) market oversight and (iv) clearing and transfer agents.

Market-Wide Initiatives

The NEP identified the following as the most significant market-wide examination priorities:

- Identifying market participants engaged in fraudulent or unethical behavior;
- Understanding firms' approaches to enterprise risk management and how they govern and manage financial, legal, compliance, operational and reputational risks;
- Looking at overall risk governance frameworks regarding the management of conflicts of interest and the sufficiency of disclosures made to investors regarding conflicts of interest; and
- Conducting examinations on supervision of information technology systems with respect to operational capability, market access, information security, risks of system outages and data integrity compromises.

Investment Adviser-Investment Company (IA-IC) Exam Program

The NEP anticipates that examinations will focus on the following ongoing risks:

- The safety of client assets and compliance with custody requirements;
- Undisclosed compensation arrangements and the conflicts of interest that they present;
- Marketing and performance advertising;
- Conflicts of interest related to the management of accounts that do not pay performance fees (e.g., most mutual funds) side-by-side with accounts that pay performance-based fees (e.g., most hedge funds); and
- Fund governance.

In addition, the staff anticipates addressing new and emerging risks for IA-ICs by:

- Launching a coordinated examination initiative designed to establish a meaningful presence with newly registered advisers;
- Continuing to expand coordinated and joint examinations with the broker-dealer program of dually registered firms and distinct broker-dealer and investment advisory businesses that share common financial professionals;

- Focusing on the growing use of alternative and hedge fund investment strategies in open-end funds, exchange-traded funds (ETFs) and variable annuity structures; and
- Focusing on payments made by advisers and funds to distributors and intermediaries, the adequacy of disclosure made to fund boards about these payments and boards' oversight of these issues.

Broker-Dealer (B-D) Exam Program

The NEP anticipates that examinations will focus on the following ongoing risks:

- Fraud in connection with sales practices regarding retail investors;
- Certain trading risk areas, with particular focus on high-frequency trading, algorithmic trading, proper controls around the use of technology, alternative trading systems and order routing practices;
- Clearing firms with multiple correspondents engaging in high-frequency/high-volume trading, focusing on the clearing firms' internal controls for managing intraday liquidity risk, as well as assessing intraday net capital and other financial risks; and
- Clearing and introducing firms that appear to have weak anti-money laundering (AML) programs, focusing on the firm's risk assessment of its business practices and implementation of the AML program related to those risks.

Moreover, the staff anticipates addressing new and emerging risks for the B-D program by:

- Focusing on firms' compliance with the Market Access Rule, with particular attention to master/sub-accounts relations, proper controls relating to proprietary trading and supervision of firms' technology system controls and governance; and
- Focusing on certain issues risks relating to ETFs (such as fails to deliver and compliance with Regulation SHO) and continuing to review the suitability of recommendations of leveraged or inverse ETFs to retail investors.

In addition to the examination priorities for the IA-IC and B-D Programs, the NEP noted various policy topics for each program such as money market funds and the JOBS Act.

Market Oversight Exam Program

Along with monitoring the activities of self-regulatory organizations (SROs) on an ongoing basis, the staff will conduct targeted, risk-focused examinations in which they will compare the effectiveness of compliance programs to an established baseline. Market Oversight will continue to review (1) SROs' obligations to enforce member compliance with financial responsibility requirements and (2) systems outages, systems errors and system integrity through SRO self-reporting. In addition, Market Oversight will inspect (1) recently registered exchanges and (2) equities exchanges to determine the types of orders available and the internal governance process around how order types are proposed, implemented and monitored. Moreover, Market Oversight will continue its efforts to enhance oversight of FINRA.

Clearance and Settlement Exam Program

The staff will conduct examinations of transfer agents and clearing agencies. With respect to its Clearing Agency Program, the staff will perform its first annual examination of Depository Trust Company, National Securities Clearing

Corporation, Fixed Income Clearing Corporation and Options Clearing Corporation in 2013, in accordance with the requirements of the Dodd- Frank Wall Street Reform and Consumer Protection Act.

Click [here](#) for the 2013 Examination Priorities.

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