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Office of Compliance Inspections and Examinations Announces its Examination Priorities for 2017

WHAT HAPPENED?	<p>The SEC’s Office of Compliance Inspections and Examinations (“OCIE”) has recently announced the 2017 examination priorities to locate potential areas of heightened risk. The OCIE will focus on three thematic areas:</p> <ul style="list-style-type: none">• Evaluating market-wide vulnerabilities;• Identifying risks for senior investors and retirement investments; and• Assessing significant issues to retail investors. <p>The OCIE’s examinations will utilize data analytics into their initiatives to locate high-risk industry practices and registrants. Through doing so, the OCIE hopes to improve its efficiency of reporting and ability to mitigate potential threats to investors.</p>
WHAT ARE THE IMPLICATIONS?	<p>The OCIE’s evaluation of market-wide risks will be based around the SEC’s goal of maintaining fair and efficient industries. The following initiatives will thus be key areas of interest:</p> <ul style="list-style-type: none">• Money Market Funds - Assessing the board’s supervision of the fund’s compliance with the October 2016 rule amendments for money market funds. Stress testing and the fund’s periodic reporting of information to the SEC are both procedures that will be key points for review.• Order Flow Payments – Certain broker-dealers will be evaluated for how they conduct best execution for customer orders.• Clearing Agencies – Annual examinations of clearing agencies for which the SEC is the supervisory agency will use a risk-based approach with the Division of Trading and Markets. This collaboration with other regulators will help to assess compliance with the Commission’s Standards for Covered Clearing Agencies.• FINRA – Conduct inspections of FINRA’s operations and regulatory programs, including their effectiveness in examining individual broker-dealers• Regulation Systems Compliance and Integrity (“SCI”) – Examine SCI entities to evaluate whether their written policies and procedures are adequately tailored for the firm’s specific operations and promote maintenance of fair and orderly markets. The OCIE’s assessment will also concentrate on how the entities record the time of transactions or events, their capacity to synchronize with

other systems, and their collection, analysis, and dissemination of market data.

- **Cybersecurity** – Assess compliance procedures for cybersecurity and how they are implemented.
- **National Securities Exchanges** – Examine operational and regulatory programs under the national securities exchanges for areas of risk.
- **Anti-Money Laundering** – Assess how broker-dealers adapt their AML programs based on current money launderings and terrorist financing risks. This assessment will also review the broker-dealer’s procedures for monitoring suspicious activity at the firm and the effectiveness of their independent testing.

A large portion of the elderly and retiring demographic are relying more on their own investments for retirement income. The OCIE will therefore expand their examination to include the following:

- **ReTIRE** – the OCIE’s multi-year ReTIRE initiative will continue to concentrate on the services provided by investment advisers and broker-dealers to investors with retirement accounts. Such services will include recommendations and sales of variable insurance products, the sales of management of target date funds, and the controls surrounding cross-transactions.
- **Public Pension Advisers** – Investment advisers to government entities like state pension plans will be examined for their abilities to manage conflicts of interest and fulfill their fiduciary duty. Other risks associated with these advisers will also be evaluated, including pay-to-play and disclosure of gifts and entertainment.
- **Senior Investors** – Firms will be assessed on their interactions with senior investors and their ability to identify any instances of financial exploitation. The registrants’ supervisory programs and management of products and services provided to senior investors will therefore be key focus points.

As the financial services industry grows and becomes increasingly complex, retail investors are exposed to a growing number of potential risks. The OCIE will thus focus on the following areas to help minimize these risks:

- **Electronic Investment Advice** – The OCIE will evaluate registered investment advisers and broker-dealers that offer automated services, like “robo-advisers”, where investment advice is provided through digital platforms. Key areas of focus will include the registrant’s compliance programs, marketing, formulation processes and algorithms used for investment recommendations, data protection, and disclosure of conflicts of interest.
- **Wrap Fee Programs** – Investment advisers will be assessed for how they uphold their fiduciary duty and fulfill contractual requirements

through wrap account suitability, effectiveness of disclosures, conflicts of interest, and brokerage practices.

- **Exchange-Traded Funds** – Examinations will review the ETF’s unit creation and redemption processes in addition to the sales practices and disclosures utilized when recommending transactions involving ETFs.
- **Never-Before Examined Investments Advisers** – The Never-Before Examined Adviser initiative will be broadened to assess both newly registered advisers and advisers who have never been examined by the OCIE but have been registered for an extended period of time.
- **Recidivist Representatives and their Employers** – Investment advisers that have employees with previous instances of misconduct, such as being subject to a regulatory action, will be examined for their compliance supervision and controls.
- **Multi-Branch Advisers** – The OCIE will proceed with its Multi-Branch Adviser Initiative to review the challenges to a compliance program and its oversight of advisory services when operating out of branch offices.
- **Share Class Selection** – Registrants will be assessed for any conflicts of interests and other related factors that influence recommendations to invest, or remain invested, in certain share classes of mutual funds. The formulation of investment recommendations and management of client portfolios will therefore be major focus points for the OCIE

Examination priorities excluded from the three main thematic areas, but are still of equal importance include the following:

- **Municipal Advisers** – The continued industry outreach, education, and assessment of municipal advisers and their compliance with the SEC and Municipal Securities Rulemaking Board rules.
- **Transfer Agents** – The review of transfers agents that service microcap issuers with an emphasis on identifying issuers who potentially engaged in unregistered, non-exempt offerings of securities.
- **Private Fund Advisers** – The examination of private fund advisers will focus on the identification and disclosure of conflicts of interest in addition to the potential benefits that advisers pursue at the expense of investors.

WHAT DOES THIS MEAN FOR ME?

The 2017 Examination Priorities announced by the OCIE is not an exhaustive list but rather continuously evolving based on market developments, conclusions from future examinations, and from collaboration with other regulators. Fairview encourages all advisers to review their business practices in regards to these examination priorities. Fairview will be working with clients to incorporate these priority items into their risk assessments

and compliance programs. If you have any questions as to potential risks related to your firm, please do not hesitate to contact Fairview.

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Sources: <https://www.sec.gov/about/offices/ocie/national-examination-program-priorities-2017.pdf>