
SEC OFFICE OF COMPLIANCE INSPECTIONS AND EXAMINATIONS PUBLISHES ITS 2020 EXAMINATION PRIORITIES

Earlier this month, the United States Securities and Exchange Commission’s Office of Compliance Inspections and Examinations (OCIE) announced its 2020 Examination Priorities and looked back at its 2019 accomplishments, in a report available [here](#).¹

OCIE completed 3,089 examinations in Fiscal Year 2019, reflecting a 2.7 percent decrease from the previous fiscal year (see Exhibit A).² Noting quality is paramount over statistics, OCIE points to the “staff’s hard work, continued improved efficiency, resiliency and dedication” to protecting investors as an illustration of its successful year, even in the face of the 35-day government shutdown where nearly all agency activities were suspended. Moreover, OCIE issued more than 2,000 deficiency letters in 2019, prompting many firms to take immediate and corrective actions, including updating policies and disclosures, or even directly returning fees to investors—more than \$70 million has been returned to investors thus far.³ 2019 examinations also resulted in 150 referrals to the Division of Enforcement.

In addition, in June 2019, the Commission finalized Regulation Best Interest, the Interpretation Regarding Standard of Conduct for Investment Advisers, and the Form CRS Relationship Summary. In 2020, OCIE will work with firms to ensure these new rules are properly implemented and strenuously followed.

Going into 2020, OCIE’s priorities are once again guided by its four pillars of promoting compliance, preventing fraud, identifying and monitoring risk, and informing policy. This year’s priorities are:

- Protection of Retail Investors
- Focus on Entities Critical to the Capital Markets Infrastructure
- Cybersecurity and Information Security Risks
- Risk-Based, Focused Exams of RIAs, RICs, BDs, and Municipal Advisors

¹ U.S. Securities and Exchange Commission, *Office of Compliance Inspections and Examinations: 2020 Examination Priorities* (Jan. 7, 2020).

² OCIE reviewed 2,180 registered investment advisers (RIAs), covering 15% of all RIAs; more than 150 investment companies; over 350 broker-dealers; 110 national securities exchanges; 90 municipal advisors and transfers agents; 160 of the Financial Industry Regulatory Authority (FINRA); and 15 clearing agencies. *Examination Priorities*, at 2.

³ This is the amount returned so far from examinations that closed in FY 2019. *Id.*, at 2-3.

- Anti-Money Laundering Compliance Programs
- Registrants Involved in Fintech, Digital Assets, and Electronic Investment Advice
- FINRA and MSRB Oversight

Protection of Retail Investors

- Examinations will focus on firms that provide advice and recommendations to retail investors, particularly those targeting investors planning for retirement, military members, and teachers.
- OCIE will work to ensure effective execution of new rules like Regulation Best Interest, which requires certain broker-dealers to act in the best interest of retail customers when recommending services.⁴ Before the June 30, 2020 deadline to implement Regulation Best Interest and Form CRS, OCIE will continue to work with broker-dealers to ensure progress on implementation and answer questions, and welcomes firms to contact the staff with questions at IABDQuestions@sec.gov. We believe that some reasonable time after the deadline, significant variations in compliance or failures to comply or attempt to comply may result in investigative referrals to the Division of Enforcement.

Protecting the Infrastructure of the Capital Markets

- OCIE will examine entities that drive or underpin the capital markets' functioning—clearing agencies, exchanges, alternative trading systems, and transfer agents.
- We believe examinations will incorporate OCIE's other priorities, such as focusing on information security systems, compliance controls, and immediacy in curing deficiencies and mitigating risks.
- OCIE will focus on examinations of national security exchanges' responses to market disruptions and compliance with federal law. Exam candidates include agents that operate in blockchain technology, microcap securities, private offerings, crowdfunded securities, or digital assets.⁵

Information and Cybersecurity

- In FY 2020, OCIE will continue to work with firms to identify and address cyber-related security issues, especially where risks may be unknown to retail investors.

⁴ While the regulation is a nod to already-existing fiduciary duties required of firms, OCIE notes this standard cannot be achieved merely through disclosure alone. To clarify the duty, the SEC published an Interpretation Regarding Standard of Conduct for Investment Advisers, which can be found [here](#). The SEC also established an inter-Divisional Standard of Conduct Implementation Committee, with members who include OCIE staff.

⁵ *Examination Priorities*, at 20.

- Regarding IRAs, OCIE will focus on six main areas relating to information security: (1) governance and risk management; (2) access controls; (3) data loss prevention; (4) vendor management; (5) training; and (6) incident response and resiliency.⁶

Added Focus Areas for RIAs, Investment Companies, Broker-Dealers, and Municipal Advisors

- OCIE’s role in examining registered investment advisers remains crucial, as assets managed by RIAs have increased from approximately \$62 trillion to \$84 trillion in the last five years.⁷ In FY 2019, OCIE examined 15% of the RIA population—2,180 firms—and will continue to examine new and not recently examined firms this year.⁸
- OCIE will prioritize examinations of RIAs that are “dually registered as, or are affiliated with, broker-dealers, or have supervised persons who are registered representatives of unaffiliated broker-dealers.”⁹
- Examinations will focus on effectiveness of compliance and control programs to inhibit risks linked to prohibited transactions, fiduciary advice, mutual fund and ETF’s RIAs, RIAs to private funds, and RIA disclosure methods.

Anti-Money Laundering Programs

- In FY 2020, OCIE will focus on examinations of broker-dealers and investment companies for compliance with anti-money laundering obligations (AML) set forth in the Bank Secrecy Act.
- In its report, OCIE notes that these examinations ensure companies have adequate safeguards in place to prevent illegal money-laundering activity.

Financial Technology and Innovation, Including Digital Assets and Electronic Investment Advice

- OCIE will continue to track industry trends and technological advancements, noting that these “risk themes” impact both retail investors and SEC-registered firms.¹⁰

⁶ *Id.*, at 13.

⁷ RIAs’ expanded reach over much of the financial market further illustrates the need for OCIE’s continued supervision, with more than 3,700 RIAs managing more than \$1 billion in assets. *Id.*, at 3.

⁸ OCIE notes these initiatives are “paying dividends,” leading to an increase in coverage from 10 percent in FY 2014 to a high in FY 2018 of 17 percent. Even with the 35-day shutdown, FY 19 coverage was 15 percent. *Id.*, at 4.

⁹ *Id.*, at 15.

¹⁰ *Id.*, at 5.

- OCIE will monitor compliance with Regulations S-P¹¹ and S-ID,¹² and focus on efforts to minimize risks linked to using third parties and vendors, including due diligence concerning cloud-based storage, online access to customer assets, and proper disposal of hardware containing client information.
- OCIE will monitor firms' preparation and disclosures concerning the transition away from LIBOR as a financial rate, particularly in relation to communications with investors.¹³
- OCIE will also focus its efforts on examining SEC-registered market participants engaged in digital assets as well as RIAs that provide services through automated tools, often called "robo-advisers."¹⁴

FINRA and MSRB

- OCIE will continue its oversight examinations of FINRA, which itself oversees approximately 3,600 brokerage firms, 630,000 registered representatives, and 156,000 branch offices.¹⁵
- OCIE develops recommendations meant to improve FINRA's process and programs. Likewise, OCIE (along with FINRA) continues to monitor MSRB policies and procedures as well as registered firms' compliance with its rules.

Conclusion and Looking Ahead

As we move into FY 2020, we will continue to watch for new developments and trends, including agency guidance and industry data as the registrant community implements Regulation BI and other recent rules. Throughout 2020, we will continue to update our clients on developments within OCIE and throughout the SEC as well as regulatory and case law developments.

¹¹ Regulation S-P mandates notice of privacy policies and opt-out rights at specific times throughout the customer relationship. See U.S. Securities and Exchange Commission, *Office of Compliance Inspections and Examinations: Risk Alert* (April 16, 2019), available [here](#).

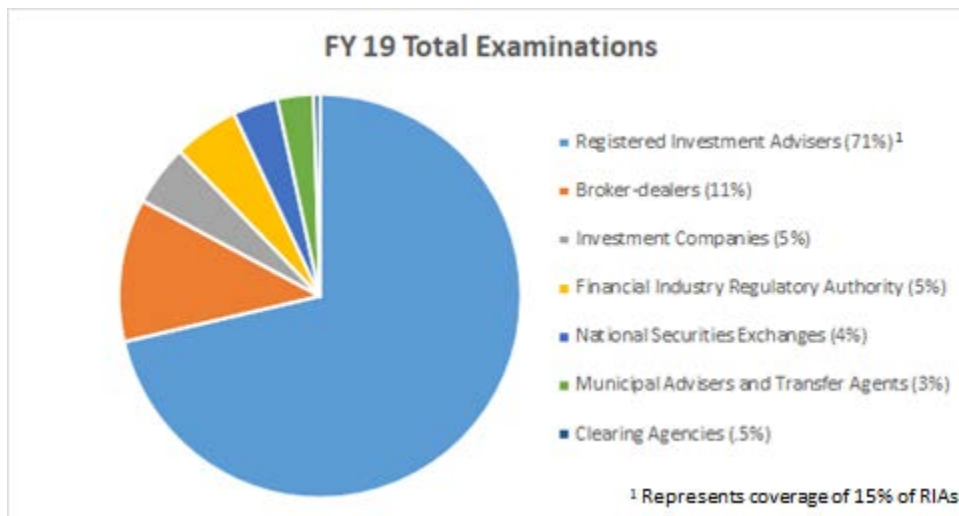
¹² Regulation S-ID provides guidelines and rules regarding effective monitoring of identity theft "red flags." For a brief compliance guide, visit [SEC Small Business Compliance Guide](#).

¹³ OCIE notes that some firms have already begun the process of evaluating the firm and client's exposure to LIBOR, including its use in accounting, risk modeling, and other areas. *Examination Priorities*, at 8-9.

¹⁴ *Id.*, at 14.

¹⁵ *Id.*, at 21.

Exhibit A –FY19 Total Examinations



If you have any questions about the information contained in this Client Alert, please contact the Thompson & Knight attorney with whom you regularly work or one of the attorneys listed below.

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