

**MEMO# 31538**

December 31, 2018

# The SEC Publishes Its 2019 Examination Priorities

[31538]

December 31, 2018 TO: ICI Members

Investment Company Directors

ICI Global Members

Chief Compliance Officer Committee

International Internal Audit Advisory Committee SUBJECTS: Anti-Money Laundering  
Compliance

Cybersecurity

Exchange-Traded Funds (ETFs)

Fixed Income Securities

Operations RE: The SEC Publishes Its 2019 Examination Priorities

The SEC's Office of Compliance Inspections and Examinations (OCIE) has published its examination priorities for 2019.[\[1\]](#) The "six themes" that OCIE plans to focus on during 2019 are:

- Matters of importance for retail investors, including seniors and retirement savers;
- Compliance and risk in registrants responsible for critical market infrastructure;
- Select areas and programs of FINRA and the MSRB;
- Digital Assets, including cryptocurrencies, coins, and tokens;
- Cybersecurity; and
- Anti-Money Laundering.

The 2019 Priorities in these areas that are relevant to mutual funds and their investment advisers are briefly summarized below.[\[2\]](#)

## Matters of Importance to Retail Investors, Seniors, and Retirement Savers

Of all the areas OCIE will focus on during 2019, this one will likely impact the Institute's members the most. The issues OCIE will focus on in this area are:

- **Fees and Expenses: Disclosure of the Cost of Investing.** Because of the impact of fees and expenses on investors' investments, OCIE will continue to review fees charged to advisory accounts to ensure that they are assessed in accordance with client agreements and firm disclosures. According to the Priorities,

For these examinations, OCIE will select firms with practices or business models that may create increased risk of inadequately disclosed fees, expenses, or other charges. **With respect to mutual fund share classes, OCIE will continue to evaluate financial incentives for financial professionals that may influence their selection of particular share classes.** In addition, OCIE remains focused on investment advisers participating in wrap fee programs, which charge investors a single bundled fee for both advisory and broker services. Continued areas of interest include the adequacy of disclosures and brokerage practices. [Emphasis added.]

- **Conflicts of Interest.** Examinations in this area will, in part, review registrants' policies and procedures relating to the use of affiliated service providers and products to assess potential conflicts relating to portfolio management practices and compensation arrangements. OCIE's focus will be on the impact to clients of any conflicts and whether they were adequately disclosed.
- **Senior Investors and Retirement Accounts and Products.** OCIE's reviews under this topic will focus on both broker-dealers and investment advisers. With respect to broker-dealers, OCIE will review how they interact with seniors and how they identify financial exploitation of seniors. With respect to investment advisers, OCIE will review the products and services offered to seniors and those investing for retirement. The focus will be on compliance programs, the appropriateness of recommendations to seniors, and the firm's supervision of its financial professionals.
- **Portfolio Management and Trading.** OCIE's focus in this area will be on ensuring that, in executing investment transactions on behalf of clients, investment advisers: are fairly allocating investment opportunities among clients; ensuring consistency of investments with the client's objectives; disclosing critical information to clients; and complying with any applicable legal restrictions.
- **Never-Before or Not Recently-Examined Investment Advisers.** This has long been a focus of OCIE. During 2019, OCIE will focus these reviews on those advisers that have not been examined for a number of years and that have substantially grown or changed business models.
- **Mutual Funds and Exchange Traded Funds.** Because mutual funds and exchange traded funds (ETFs) are the primary investment vehicle for many retail investors, OCIE plans to continue to prioritize examinations of these funds, their advisers, and their boards of directors. These reviews will assess industry practices and regulatory compliance "in various areas that may have significant impact on retail investors." OCIE will particularly focus on:[\[3\]](#)
  - Index funds that track custom-built or bespoke indexes;
  - ETFs with little secondary market trading volume or smaller assets under management;
  - Funds with higher allocation to certain securitized assets;
  - Funds with aberrational underperformance relative to their peer groups;
  - Funds that are managed by advisers that are relatively new to managing registered investment companies; and
  - Advisers that provide advice to both registered and private funds with similar investment strategies.

## **Compliance and Risk in Registrants Responsible for Critical Market Infrastructure**

Under this topic, among other things, OCIE plans to examine transfer agents to assess “transfers, recordkeeping, and the safeguarding of funds and securities.” These reviews will also focus on compliance with transfer agents’ obligation to annually file a report by an independent public accountant concerning the transfer agency’s system of internal account controls.

## **Digital Assets**

The growth and potential risks to retail investors associated with digital assets make this area a focus of OCIE. According to the Priorities, in reviewing broker-dealers, trading platforms, and investment advisers involved with digital assets,

. . . through high level inquiries, OCIE will take steps to identify market participants offering, selling, trading, and managing these products or considering or actively seeking to offer these products and then assess the extent of their activities. For firms actively engaged in the digital asset market, OCIE will conduct examinations focused on, among other things, portfolio management of digital assets, trading, safety of client funds and assets, pricing of client portfolios, compliance, and internal controls.

## **Cybersecurity**

OCIE plans to continue to prioritize cybersecurity as part of its examination program. As expressed in the Priorities:

Examinations will focus on, among other things, proper configuration of network storage devices, information security governance generally, and policies and procedures related to retail trading information security. Specific to investment advisers, OCIE will emphasize cybersecurity practices at investment advisers with multiple branch offices, including those that have recently merged with other investment advisers, and continue to focus on, among other areas, governance and risk assessment, access rights and controls, data loss prevention, vendor management, training, and incident response.

## **Anti-Money Laundering Programs**

OCIE’s examinations relating to AML compliance will focus on broker dealers and whether their AML programs comply with all applicable regulatory requirements including SAR filing obligations and the independent testing of their AML program in a timely and robust fashion.

While these Priorities “provide a preview of where OCIE intends to focus its limited resources,” they are not an exhaustive list of all areas that OCIE will cover in examinations. Also, while OCIE has prioritized the above areas for review, it will adjust its risk-based program as necessary due to changes in the markets and investor needs and preferences. The Priorities additionally note OCIE’s plans to continue to leverage technology and data analytics during 2019 to increase its efficiency.

Tamara K. Salmon  
Associate General Counsel

## endnotes

[1] See *2019 Examination Priorities*, Office of Compliance Inspections and Examinations, US Securities and Exchange Commission (December 20, 2018), which is available at: <https://www.sec.gov/files/OCIE%202019%20Priorities.pdf> (the “Priorities”).

[2] Omitted from this summary is the discussion in the Priorities relating to “Focus on FINRA and MSRB.”

[3] According to the Institute’s members, the reviews discussed in the first three bullets began in 2018.

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