

SEC Announces 2016 Examination Priorities for Private Fund Managers

On January 11, 2016, the SEC's Office of Compliance Inspections and Examinations ("OCIE") published its [Examination Priorities for 2016](#), including:

- a continued concentration on private fund managers,¹ including never-before-examined investment advisers and a continued focus on fees and expenses.²
- a focus on private placements, including Regulation D offerings, to evaluate whether legal requirements are being met in the areas of due diligence, disclosure, and suitability. Accordingly, private fund managers may receive scrutiny on policies and procedures relating to private placements, as well as past practices. This could include inquiries into whether or not an offering potentially involved a general solicitation, the fund manager's procedures regarding the establishment of pre-existing relationships with offerees before making an offer, "accredited investor" qualification of investors, timely Form D or other filings (where required) and related issues.
- a focus on cybersecurity, including testing and assessments of firms' implementation of procedures and controls. This continues OCIE's previously announced focus on cybersecurity,³ and follows on the heels of a recent enforcement action against a private fund manager for failure to adopt cybersecurity controls.⁴
- for managers of hedge funds and other more liquid vehicles and strategies, a focus on liquidity controls, particularly in cases where funds have exposure to potentially illiquid fixed income securities. In those cases, OCIE expects to scrutinize controls over market risk management, valuation, liquidity management, trading activity and other related matters. While this would presumably be less relevant for managers of funds that do not permit investor redemptions, OCIE would likely find it relevant for funds that do permit investor redemptions. Managers of open-ended funds should therefore expect exam focus on these issues.
- a focus on anti-money laundering in the context of OCIE's examinations of broker-dealer firms.⁵ The 2016 Examination Priorities are silent as to any similar focus in the context of private fund managers or other investment advisers. However, the Financial Crimes Enforcement Network recently proposed anti-money laundering rules for private fund managers and other investment advisers, and OCIE has recommended the adoption of anti-money laundering policies in previous exams of private fund managers. Accordingly, although not yet an announced focus area for private fund managers, it is possible that OCIE may devote some attention to this topic in future exams.

In announcing these and other⁶ priorities, OCIE noted that its list was not exhaustive, and that it also intends to conduct examinations focused on risks, issues, and policy matters that arise from market developments, new information learned from examinations or other sources, including tips, complaints, and referrals, and coordination with other regulators.

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- 1 Although not highlighted in the 2016 Examination Priorities, a senior staff member of the SEC recently stated that OCIE may begin to examine exempt reporting advisers (i.e., investment advisers that have claimed an exemption from Advisers Act registration under the so-called mid-sized private fund adviser or venture capital fund exemptions).
 - 2 OCIE also stated that it would focus on the controls and disclosure associated with side-by-side management of performance-based and purely asset-based fee accounts. While not relevant for all private fund managers, this issue will be relevant to those managing multiple fund vehicles and/or managed accounts that follow the same or similar investment programs but are subject to differing compensation arrangements.
 - 3 See [OCIE National Exam Program Risk Alert: OCIE's 2015 Cybersecurity Examination Initiative](#), September 15, 2015.
 - 4 See September 24, 2015 *Kirkland AIM*, "[SEC Brings Cybersecurity Enforcement Action Against Registered Adviser](#)," for further analysis of this topic, as well as the [SEC Consent Order](#) and [Press Release](#).
 - 5 OCIE expects to use its data analytics capabilities to assess whether a broker-dealer being examined had filed the statistically-expected number of suspicious activity reports required under the rules applicable to broker-dealers. OCIE also noted separately that it would continue to assess the sufficiency and degree of customization of broker-dealers' anti-money laundering policies, as well as the sufficiency of their internal testing.
 - 6 OCIE also plans to scrutinize advisers to municipalities and other government entities, "focusing on pay-to-play and certain other key risk areas related to advisers to public pensions, including identification of undisclosed gifts and entertainment." This line of inquiry may lead to focus in exams of private fund managers that have accepted public pension plans as investors. Potential areas of inquiry in such cases may include marketing practices (including gifts and entertainment) directed to public pension plans and their intermediaries. Intermediaries that serve as primary advisers to public pension plans may also receive examination focus on this topic. In addition, although not highlighted in the 2016 Examination Priorities, the fact that 2016 is an election year may increase the amount of political contribution activity among fund manager personnel. Accordingly, investment advisers should remain vigilant in monitoring political contributions and political fundraising activity by covered personnel.

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