

U.S. SECURITIES AND
EXCHANGE COMMISSION

2022

EXAMINATION PRIORITIES

Division of Examinations

DISCLAIMER: This statement represents the views of the staff of the Division of Examinations. It is not a rule, regulation, or statement of the U.S. Securities and Exchange Commission (SEC). The Commission has neither approved nor disapproved its content. This statement, like all staff guidance, has no legal force or effect: it does not alter or amend applicable law, and it creates no new or additional obligations for any person. This document was prepared by the Division of Examinations and is not legal advice.

CONTENTS

Division of Examinations' Leadership Message.....	1
Fiscal Year 2021	3
A Word About "Compliance"	6
Final Notes	8
DIVISION OF EXAMINATIONS – 2022 EXAMINATION PRIORITIES	9
I. Significant Focus Areas.....	11
A. Private Funds.....	11
B. Environmental, Social, and Governance (ESG) Investing.....	12
C. Standards of Conduct: Regulation Best Interest, Fiduciary Duty, and Form CRS.....	13
D. Information Security and Operational Resiliency	15
E. Emerging Technologies and Crypto-Assets	16
II. Investment Adviser and Investment Company Examination Program.....	17
A. Registered Investment Advisers	17
B. Registered Investment Companies, Including Mutual Funds and ETFs	18
III. Broker-Dealer and Exchange Examination Program.....	19
A. Microcap, Municipal, Fixed Income, and Over-The-Counter Securities.....	19
B. Broker-Dealer Operations	20
C. National Securities Exchanges	20
D. Security-Based Swap Dealers (SBSDs)	21
E. Municipal Advisors	21
F. Transfer Agents	21
IV. Clearance and Settlement Examination Program.....	22
V. Regulation Systems Compliance and Integrity.....	22
VI. FINRA	23
VII. MSRB	24
VIII. The London Inter-Bank Offered Rate (LIBOR) Transition	24
IX. Anti-Money Laundering.....	25
X. Conclusion	26



DIVISION OF EXAMINATIONS' LEADERSHIP MESSAGE

The Division of Examinations is pleased to share our examination priorities for fiscal year (FY) 2022. Last year, we acknowledged two important exam milestones, the elevation of the Office of Compliance Inspections and Examinations to the Division of Examinations and the 25th anniversary of a stand-alone examination program. This year, we mark another important milestone – a decade of publishing the Division's examination priorities.



The annual publication of our examination priorities furthers the SEC's mission and aligns with the Division's four pillars to promote and improve compliance, prevent fraud, monitor risk, and inform policy. The examination priorities have taken on greater prominence over the years and have become an important tool for the examination program. The publication of the examination priorities provides investors and registrants transparency into those areas we believe bring heightened risks to investors, registrants, and the markets.

If you were to review the Division's first priorities from February 2013, you might notice its relative brevity. But upon closer inspection, you would see that many of today's priorities address topics and themes similar to those that the examination program was prioritizing in 2013, and likely many years in between. These perennial priorities represent fundamental obligations under the federal securities laws and are frequently at the core of SEC-registrant operations. For example, the 2013 priorities included a focus on high risk areas such as conflicts of interest, disclosures of fees and expenses, safety of investor and client assets, sales practices, and oversight of systemically important and similarly situated organizations that are essential to the fair and orderly operation of our markets. And although the word "cyber" was not used until 2014, risks related to data compromises were highlighted as well as what has become a perennial focus on addressing the impact and governance surrounding the use of new and emerging technologies across registrant types.

Not all priorities are perennial, however. Each year, in developing our examination priorities, we engage in a deliberative process across the SEC to identify the areas we believe exhibit the highest risks to investors and the markets or are trending in that direction. Some areas take on more or less prominence in our examinations as the markets, technology, regulation, services provided to investors, and investor preferences evolve. However, it is important to note that as our priorities evolve, it does not mean we are no longer conducting examinations in areas not specifically noted in our priorities. Published priorities are not exhaustive, nor do they represent the only areas we will consider in assessing and identifying examination candidates.

Underpinning the last decade of published priorities is the desire to be transparent about the heightened risks that we see, to highlight many of the areas examinations will focus on in the year ahead, and ultimately to protect investors, prevent fraud, and promote and improve compliance. We hope that firms' leadership, including those in compliance, legal, risk, and information security, across the financial services industry will review the priorities and consider their firms' operations and internal controls in these higher-risk areas to avoid potential compliance weaknesses or failures.

Fiscal Year 2021

The Division completed 3,040 examinations in FY21, a 3% increase from FY20 and about on par with pre-Covid-19 pandemic examination totals in FY19. In addition to examinations, the staff conducted hundreds of registrant outreach meetings to monitor several very significant market events, including the volatility in the equity and options markets in early 2021 that touched on several of our program areas. And although numbers are just part of the story, underpinning the great exam numbers for FY21 is the continued perseverance of the staff of the Division and their unwavering commitment to the SEC's and the Division's mission to protect investors. We are incredibly proud of the staff's continued efforts this past year to perform meaningful examinations remotely while contending with the on-going impacts of the Covid-19 pandemic.

During FY21, the Division issued more than 2,100 deficiency letters. Through these letters, we have our most direct impact improving and promoting compliance and investor protection and addressing market risk. Most firms, as a result of the deficiency letters we issue, take steps to remediate the staff's findings. Frequently, remediation includes implementing changes to policies and procedures so they are more effective, updating regulatory filings so they are more clear and responsive, or improving the quality of disclosures made to investors to be more transparent. Deficiency letters have also prompted some firms to return fees and other charges back to investors and make corrections in how they were calculating those fees. To date, our FY21 examinations prompted firms to return more than \$45M to investors. The Division also made more than 190 referrals of its examination findings to the Division of Enforcement. As we move further into FY22, we anticipate there will be more money returned to investors, and there will be additional referrals to Enforcement resulting from our FY21 examinations.

The Investment Adviser/Investment Company (IA/IC) Examination Program, the Division's largest program, completed more than 2,200 examinations of investment advisers in FY21, an increase from both FY20 and FY19. It also completed over 125 examinations of investment company complexes. In addition to the number of exams, an important metric is the percentage of SEC-registered investment advisers we examine each year. As the primary and often only regulator responsible for the oversight of this cohort of registrants,

we closely track our coverage ratio and have targeted it to be 15% for the past several years. This year, the Division examined approximately 16% of RIAs, compared to 15% in FY20 and FY19. Although there was a slight increase in the coverage percentage in FY21, we will likely soon have to lower our annual coverage target as the growth in the number of RIAs continues to grow at a rate that far outpaces staffing increases. In FY21, we saw some of the fastest year-over-year growth ever, with a net addition of approximately 900 RIAs. And over the last five years, the number of RIAs has increased 20%, from approximately 12,250 to over 14,800.

The growth in the numbers of RIAs does not fully capture the increasing complexity of the asset management industry, and the resulting increased complexity of the compliance issues and risks covered by our examinations. For instance, the number of RIAs with AUM over \$10 billion has increased by 30% in the past five years alone, and total AUM is now over \$113 trillion, itself a nearly 70% increase from five years ago. In addition, approximately 60% of RIAs are affiliated with other financial industry firms, and more than 35% manage a private fund.

The Division's Broker-Dealer and Exchange Examination Program continued to conduct examinations focused on broker-dealers' compliance with Regulation Best Interest, wrapping up its initial exams to look for good faith compliance and kicking off the second phase of examinations with additional review of effectiveness of policies and procedures and transaction testing. In addition to the oversight of broker-dealers, BDX conducts examinations of municipal advisors, national securities exchanges, and transfer agents. The program completed nearly 450 examinations of these registrants in FY21.

The FINRA and Securities Industry Oversight (FSIO) Examination Program completed more than 115 examinations of FINRA in FY21, including examinations of key FINRA oversight areas, and held frequent monitoring meetings with FINRA on various aspects of its operations to assess and identify risk areas in these operations.

The Clearance and Settlement Examination Program conducted 15 examinations of clearing firms, including critically important work around the Systemically Important Financial Market Utilities (or SIFMUs). And our Technology Controls Program (TCP) completed 81 examinations, including examinations of entities subject to Regulation Systems Compliance and Integrity (SCI), RIAs and broker-dealers.

The Division also maintained its focus on transparency and support of compliance through outreach events and publications. Division staff participated in more than 150 conferences and outreach events, including a national outreach event for municipal advisors in October and regional outreach events for IA and IC compliance officers. We continued to maintain a steady pace of issuing Risk Alerts throughout the year as well. In FY21, the Division published nine Risk Alerts across a variety of topics. These Risk Alerts are designed to raise awareness of compliance and industry risks and are meant to encourage firms to think about their own policies and procedures in particular areas. The FY21 Risk Alerts include:

- Observations from Examinations of Investment Advisers: Supervision, Compliance and Multiple Branch Offices
- Investor Adviser Compliance Programs
- Observations from Examinations of Broker-Dealers and Investment Advisers: Large Trader Obligations
- Executive Order on Securities Investments that Finance Communist Chinese Military Companies
- The Division of Examinations' Continued Focus on Digital Asset Securities
- Compliance Issues Related to Suspicious Activity Monitoring and Reporting at Broker-Dealers
- The Division of Examinations' Review of ESG Investing
- Observations from Examinations of Investment Advisers Managing Client Accounts that Participate in Wrap Fee Programs
- Observations Regarding Fixed Income Principal and Cross Trades by Investment Advisers from an Examination Initiative

We intend to continue publishing Risk Alerts, providing observations from examinations and alerting the industry to potentially new compliance and market risks. We take our role to promote compliance to mean that part of our job is to raise awareness of compliance risks and share practices that aided an effective compliance strategy.

A Word About “Compliance”

With our name change last year to the Division of Examinations, some have speculated that the removal of “compliance” from the Division’s name was intended to deemphasize our long-standing focus on, and commitment to, promoting compliance and to empowering compliance officers. Rest assured, that is not the case.

The importance of improving and promoting compliance remains at the forefront of the Division’s work. We engage with Chief Compliance Officers and compliance staff routinely on each examination. In addition, we have continued to look for opportunities to engage with compliance professionals and the compliance community through various outreach initiatives. For example, as noted above, we conduct several national and regional compliance outreach programs each year for a variety of registrant types, and publish our priorities, Risk Alerts and other reports to provide transparency on many areas directly tied to compliance.

While many registrants demonstrate the value and importance they place on compliance, far too often we examine registrants where that is not the case. In last year’s leadership message we highlighted compliance engagement across business lines, knowledgeable Chief Compliance Officers, and firm principals’ commitment to compliance. It bears repeating—compliance officers must be empowered and receive support in the form of resources and a tone from the top that recognizes their contributions. Senior officers and executives empower compliance and compliance officers through their words and actions.

Another characteristic of an effective compliance program is resiliency, which has never been more apparent as we all continue to address pandemic-related change. Compliance programs and the written policies and procedures that embody them should be developed and designed to continue to be effective and withstand changes in, for example, market conditions, investor demand, key personnel, and registrant services or lines of business. A well-designed and resilient compliance program and compliance staff should be able to adjust, pivot, and address a range of conditions and scenarios.

In performing examinations, we have observed several commonalities of resilient compliance programs.

Inclusivity

The primary responsibility to develop and maintain a compliance program may be with the Chief Compliance Officer and others in a compliance department, but for most firms the foundation of a resilient compliance program requires participation

and input across all business and operational lines. Staff from across a firm working in collaboration with compliance can bring additional expertise and diverse perspectives to the development of a compliance program and the design of effective controls. Additional benefits, including a sense of shared ownership and greater attention to implementation, can also result from an inclusive approach to compliance.

Change Management

A well thought out and well-designed compliance program will be flexible enough to adjust to known variables in operations and business, but will also have established processes in place to monitor effectiveness and to pivot or be updated when appropriate. As we have all experienced over the last couple of years, significant unanticipated events can occur as well as more incremental change that can compound over time or across operational lines, causing once effective policies and procedures or controls to become weak or ineffective. Compliance programs and related policies and procedures are not “set it and forget it” endeavors, and having a process in place to address new compliance risks and challenges is critical to resiliency.

Reviews and Testing

Periodic review and testing of policies and procedures is necessary to ensure the on-going adequacy and effectiveness of a compliance program. As the Commission has noted in the context of investment adviser compliance programs, reviews should consider compliance matters that arose previously, changes in business activities, and regulatory changes. Testing is also critical, as it provides a means to affirm that policies and procedures are operating as designed and to ensure the detection of outlier events or unusual patterns. An effective testing program, such as one that includes testing on a routine periodic basis at set intervals, when certain transactions occur, and over extended periods to look for patterns or emerging trends, deployed in conjunction with periodic reviews, significantly contributes to the on-going resiliency of a compliance program.

We fully anticipate that our focus on compliance, support of compliance, and compliance empowerment will continue and we look forward to continued engagement with the compliance community in the year to come.

Final Notes

Perhaps the most significant storyline of FY21 for the Division was the continued impact of the Covid-19 pandemic on us and the financial services industry generally. As we look back on the Division's results from the previous year and plan for the new initiatives and focus areas for the year to come, the theme of resiliency again comes to mind. Specifically, the resiliency of the Division's systems and controls, the resiliency of our operating posture and capacity, but most importantly, the resiliency of the 1000 plus person staff that make up the examination program. Their tenacity, commitment to mission and public service, and collaborative spirit is really the crowning achievement for the year. We are certain many firms share a similar sentiment for their own employees and the resiliency they have demonstrated.

Finally, the past year has brought change to the Division. We established the Office of Security-Based Swaps to carry out the Division's oversight responsibilities for security-based swaps entities registered with the Commission, including security-based swaps dealers, and to coordinate and collaborate with our colleagues in the Division of Trading and Markets and other offices and divisions as part of the newly launched Security-Based Swaps Joint Venture. We examined registrants for compliance for several new regulations, including amendments to Regulation NMS Rule 606 and the Investment Company Liquidity Risk Management Program Rule. And last, there was change in the senior leadership ranks of the Division with the departure of Director Pete Driscoll, Acting Director and Chief Counsel Dan Kahl, Deputy Director and co-head of the IA/IC examination program Kristin Snyder, and head of the Clearance and Settlement program Dan Gregus. We thank them for their service, and are fortunate that there are many great leaders in the Division to fill these gaps, including Joy Thompson, Natasha Greiner, and Lourdes Caballes who are currently leading as Deputy Director, co-head of the IA/IC examination program, and head of the Office of Clearance and Settlement, respectively.

The Division's contact information can be found at <https://www.sec.gov/contact-information/sec-directory>. If you suspect or observe activity that may violate the federal securities laws or otherwise operates to harm investors, please notify SEC staff at <https://www.sec.gov/tcr>. We welcome engagement between our staff and members of the public, and we appreciate hearing from the industry about new and emerging risk areas, products, and services.

Division of Examinations

2022

**EXAMINATION
PRIORITIES**



The Division of Examinations (Division or EXAMS) prioritizes examination of certain practices, products, and services that it believes present potentially heightened risks to investors or the integrity of the U.S. capital markets. Examinations of these priority areas are grounded in our four pillars: promoting compliance, preventing fraud, identifying and monitoring risk, and informing policy. Collectively, examinations and our other efforts, including publication of Risk Alerts and industry and investor outreach, are designed to support the SEC's mission to protect investors, facilitate capital formation, and maintain fair, orderly, and efficient markets.

The Division will prioritize examinations of several significant focus areas that pose unique or emerging risks to investors or the markets, as well as examinations of core and perennial risk areas. Their importance to investors and the markets, coupled with the seriousness and frequency of observations in prior years' examinations, demonstrate the need for the Division to remain vigilant in these areas. And while all of the areas identified below are critical, this list of priorities is not comprehensive and these will not be the only issues the Division addresses in examinations, Risk Alerts, and industry and investor outreach. The Division continues to be flexible so that examinations may also cover new and exigent risks to investors and the marketplace as they arise.

I. SIGNIFICANT FOCUS AREAS

A. Private Funds

More than 5,000 SEC-registered investment advisers (RIAs), totaling over 35% of all RIAs, manage approximately \$18 trillion in private fund assets deployed in a variety of investment strategies in various fund types, including hedge funds, private equity funds, and real estate funds. These private funds frequently have significant investments from state and local pensions with working family beneficiaries, charities, and endowments. The size and complexity of these RIAs vary widely from, for example, an adviser with a small closely-held private fund to an adviser managing hundreds of billions of dollars across multiple types of funds and strategies. In the past five years, there has been a 70% increase in the assets managed by advisers to private funds.

DID YOU KNOW?

In the past five years, there has been a 70% increase in the assets managed by advisers to private funds.

Given the significance of examination findings over the past several years, and the size, complexity, and significant growth of this market, the Division will continue to prioritize our focus on RIAs to private funds. Examinations will review issues under the Investment Advisers Act of 1940 (Advisers Act), including an adviser’s fiduciary duty, and will assess risks, including a focus on compliance programs, fees and expenses, custody, fund audits, valuation, conflicts of interest, disclosures of investment risks, and controls around material nonpublic information (MNPI).

Specifically, EXAMS will continue to review: (1) the calculation and allocation of fees and expenses, including the calculation of post-commitment period management fees and the impact of valuation practices at private equity funds; (2) the potential preferential treatment of certain investors by RIAs to private funds that have experienced issues with liquidity, including imposing gates or suspensions on fund withdrawals; (3) compliance with the Advisers Act Custody Rule, including the “audit exception” to the surprise examination requirement and related reporting and updating of Form ADV regarding the audit and auditors that serve as important gate-keepers for private fund investors; (4) the adequacy of disclosure and compliance with any regulatory requirements for cross trades, principal transactions, or distressed sales; and (5) conflicts around liquidity, such as RIA-led fund restructurings, including stapled secondary transactions where new investors purchase the interests of existing investors while also agreeing to invest in a new fund.

The Division will also review private fund advisers’ portfolio strategies, risk management, and investment recommendations and allocations, focusing on conflicts and disclosures around these areas. This will include, for example, review of private funds’ investments in Special Purpose Acquisition Companies (SPACs), particularly where the private fund adviser is also the SPAC sponsor. In addition, EXAMS will review the practices, controls, and investor reporting around risk management and trading for private funds with indicia of systemic importance, such as outsized counterparty exposure or gross notional exposure when compared to similarly situated firms.

B. Environmental, Social, And Governance (ESG) Investing

RIAs and registered funds are increasingly offering and evaluating investments that employ ESG strategies or incorporate certain ESG criteria, in part to meet investor demand for such strategies and investments. There is a risk that disclosures regarding portfolio management practices could involve materially false and misleading statements or omissions, which can result in misinformed investors. This risk may be compounded by: (1) the lack of standardization in ESG investing terminology (*e.g.*, strategies that are referred to as sustainable, socially responsible, impact investing, and environmental, social,

and governance conscious, which incorporate ESG criteria); (2) the variety of approaches to ESG investing (*e.g.*, a portfolio may be labeled as ESG because of consideration of ESG factors alongside traditional financial, industry-related, and macroeconomic indicators, among others; other portfolios may use ESG factors as the driving or main consideration in selecting investments; or some portfolios engage in impact investing seeking to achieve measurable ESG impact goals); and (3) the failure to effectively address legal and compliance issues with new lines of business and products.

The Division will continue to focus on ESG-related advisory services and investment products (*e.g.*, mutual funds, exchange-traded funds (ETFs), and private fund offerings). Such reviews will typically focus on whether RIAs and registered funds are: (1) accurately disclosing their ESG investing approaches and have adopted and implemented policies, procedures, and practices designed to prevent violations of the federal securities laws in connection with their ESG-related disclosures, including review of their portfolio management processes and practices; (2) voting client securities in accordance with proxy voting policies and procedures and whether the votes align with their ESG-related disclosures and mandates; or (3) overstating or misrepresenting the ESG factors considered or incorporated into portfolio selection (*e.g.*, greenwashing), such as in their performance advertising and marketing.

C. Standards of Conduct: Regulation Best Interest, Fiduciary Duty, and Form CRS

The Division will continue to address standards of conduct issues for broker-dealers and RIAs, with reviews focused on how they are satisfying their obligations under Regulation BI and the Advisers Act fiduciary standard to act in the best interests of retail investors and not to place their own interests ahead of retail investors' interests. Examinations will include assessments of practices regarding consideration of alternatives (*e.g.*, with regard to potential risks, rewards, and costs), management of conflicts of interest (*e.g.*, incentive practices that favor certain products or strategies over others), trading (*e.g.*, RIA best execution obligations), disclosures (*e.g.*, disclosures provided in Form ADV and Form CRS and made pursuant to Regulation BI), account selection (*e.g.*, brokerage, advisory, or wrap fee accounts), and account conversions and rollovers. For both broker-dealers and RIAs, examinations will focus on the effectiveness of compliance programs, testing, and training that are designed to support retail investors and working families receiving recommendations and advice in their best interests.

DID YOU KNOW?

The Division will continue to address standards of conduct issues for broker-dealers and RIAs, with reviews focused on how they are satisfying their obligations under Regulation BI and the Advisers Act fiduciary standard to act in the best interests of retail investors and not to place their own interests ahead of retail investors' interests.

Broker-dealer examinations will review firms' recommendations and sales practices related to SPACs, structured products, leveraged and inverse exchange traded products (ETPs), REITs, private placements, annuities, municipal and other fixed income securities, and microcap securities. Examinations will review practices, policies, and procedures concerning the evaluation of cost and reasonably available alternatives as they relate to recommendations of these products being in the investor's best interest. Examinations will also evaluate the compensation structures for financial professionals, including the conflicts created by such structures, and may focus examinations on the sales of securities by financial professionals that are highly compensated.

RIA examinations will focus on whether advisers are acting consistently with their fiduciary duty to clients, looking at both duties of care and loyalty, including best execution obligations, financial conflicts of interest and related impartiality of advice, and any attendant client disclosures. Focus areas include: (1) revenue sharing arrangements; (2) recommending or holding more expensive classes of investment products when lower cost classes are available (*e.g.*, RIAs that recommend no transaction fee mutual fund share classes that have 12b-1 fees in wrap fee accounts where the RIA may be responsible for paying transaction fees); (3) recommending wrap fee accounts without assessing whether such accounts are in the best interests of clients, including the impact of the move to zero commissions on certain types of securities transactions by a number of broker-dealers; and (4) recommending proprietary products resulting in additional or higher fees. Such reviews also will include an assessment of the adequacy of RIAs': (1) compliance policies and procedures designed to address conflicts and ensure advice in the best interest of clients, including the cost of investing; and (2) disclosures to enable investors to provide informed consent.

Dually registered RIAs and broker-dealers remain an area of interest for the Division, as do affiliated firms with financial professionals who service both brokerage customers and advisory clients. The focus areas of such examinations will be similar to those addressed above, but with particular emphasis on potential conflicts of interest present at these firms, including with regard to account recommendations and allocation of investments across different accounts. For example, examinations will include a focus on: (1) the sale or recommendation of high fee products; (2) the sale or recommendation of proprietary products of the firms or their affiliates; (3) incentives for financial professionals to place their own or their firms' interests ahead of customers/clients (*e.g.*, transactions that reduce costs to the adviser and increase expenses borne by the client); and (4) compensation structures that inappropriately influence investment recommendations. The Division will review whether these firms have implemented written policies and procedures to effectively

mitigate and address conflicts and to minimize the risk of, and monitor for, misaligned incentives that may result in recommendations and advice to retail investors, such as seniors and working families that is not in their best interest.

D. Information Security and Operational Resiliency

Applying information security controls is critical to ensuring business continuity. Vigilant protection of data is also critical to the operation of the financial markets and the confidence of its participants. Failing to prevent unauthorized access, use, disclosure, disruption, modification, inspection, recording or destruction of sensitive records may have consequences that extend beyond the firm compromised to other market participants and retail investors. Accordingly, the Division will review broker-dealers' and RIAs' practices to prevent interruptions to mission-critical services and to protect investor information, records, and assets.

Specifically, EXAMS will continue to review whether firms have taken appropriate measures to: (1) safeguard customer accounts and prevent account intrusions, including verifying an investor's identity to prevent unauthorized account access; (2) oversee vendors and service providers; (3) address malicious email activities, such as phishing or account intrusions; (4) respond to incidents, including those related to ransomware attacks; (5) identify and detect red flags related to identity theft; and (6) manage operational risk as a result of a dispersed workforce in a work-from-home environment. In the context of these examinations, the Division will focus on, among other things, broker-dealers' and RIAs' compliance with Regulations S-P and S-ID, where applicable.

The Division will again be reviewing registrants' business continuity and disaster recovery plans, with particular focus on the impact of climate risk and substantial disruptions to normal business operations. As the Division described last year, these efforts build on previous examinations and outreach in this area. In some cases, particularly in regard to systemically important registrants, examinations will account for certain climate related risks. The scope of these examinations will include a focus on the maturation and improvements to business continuity and disaster recovery plans over the years as well as these registrants' resiliency as organizations to anticipate, prepare for, respond to, and adapt to both sudden disruptions and incremental changes stemming from climate-related situations.

DID YOU KNOW?

The Division will again be reviewing registrants' business continuity and disaster recovery plans, with particular focus on the impact of climate risk and substantial disruptions to normal business operations.

E. Emerging Technologies and Crypto-Assets

The Division has observed a significant increase in the number of RIAs choosing to provide automated digital investment advice to their clients (often referred to as “robo-advisers”), continued growth in the use of mobile apps by broker-dealers, and a proliferation of the offer, sale, and trading of crypto-assets. The Division will conduct examinations of broker-dealers and RIAs that are using developing financial technologies to review whether the unique risks these activities present were considered by the firms when designing their regulatory compliance programs.

DID YOU KNOW?

The Division will conduct examinations of broker-dealers and RIAs that are using developing financial technologies to review whether the unique risks these activities present were considered by the firms when designing their regulatory compliance programs.

RIA and broker-dealer examinations will focus on firms that are, or claim to be, offering new products and services or employing new practices (*e.g.*, fractional shares, “Finfluencers,” or digital engagement practices) to assess whether: (1) operations and controls in place are consistent with disclosures made and the standard of conduct owed to

investors and other regulatory obligations; (2) advice and recommendations, including by algorithms, are consistent with investors’ investment strategies and the standard of conduct owed to such investors; and (3) controls take into account the unique risks associated with such practices.

Examinations of market participants engaged with crypto-assets will continue to review the custody arrangements for such assets and will assess the offer, sale, recommendation, advice, and trading of crypto-assets. In particular, EXAMS will review whether market participants involved with crypto-assets: (1) have met their respective standards of conduct when recommending to or advising investors with a focus on duty of care and the initial and ongoing understanding of the products (*e.g.*, blockchain and crypto-asset feature analysis); and (2) routinely review, update, and enhance their compliance practices (*e.g.*, crypto-asset wallet reviews, custody practices, anti-money laundering reviews, and valuation procedures), risk disclosures, and operational resiliency practices (*i.e.*, data integrity and business continuity plans). In addition, the Division will conduct examinations of mutual funds and ETFs offering exposure to crypto-assets to assess, among other things, compliance, liquidity, and operational controls around portfolio management and market risk.

II. INVESTMENT ADVISER AND INVESTMENT COMPANY EXAMINATION PROGRAM

A. Registered Investment Advisers

During a typical examination, the Division reviews the compliance programs of RIAs in one or more of the following core areas: marketing practices, custody and safety of client assets, valuation, portfolio management, brokerage and execution, conflicts of interest, and related disclosures. The Division will assess whether policies and procedures are reasonably designed to prevent violations of the Advisers Act and its rules, including breaches of the RIA's fiduciary duty in violation of the antifraud provisions. Additionally, EXAMS will review compliance programs to examine whether they address that: (1) investment advice is in each client's best interest; (2) oversight of service providers is adequate; and (3) sufficient resources exist to perform compliance duties. In addition, to the extent that firms are using alternative data or data gleaned from non-traditional sources as part of their business and investment decision-making processes, reviews will include examining whether RIAs, including RIAs to private funds and registered funds, are implementing appropriate compliance and controls around the creation, receipt, and use of potentially MNPI.

As part of its assessment of the effectiveness of a compliance program, the Division will review whether the firm has implemented oversight practices to mitigate any heightened risks. For example, whether RIAs: (1) employing individuals with prior disciplinary histories implemented heightened oversight practices for these individuals; (2) migrating from the broker-dealer business model reviewed whether recommendations to transition investor accounts to advised accounts were in the clients' best interests; and (3) operating from multiple branch offices have appropriately adapted their compliance programs to oversee the activities in their branches.

The Division will also continue to focus on RIA disclosures and other issues related to fees and expenses. In particular, EXAMS will concentrate on issues associated with: (1) advisory fee calculation errors, including, but not limited to, failure to adjust management fees in accordance with investor agreements; (2) inaccurate calculations of tiered fees, including failure to provide breakpoints and aggregate household accounts; and (3) failures to refund prepaid fees for terminated accounts or pro-rated fees for onboarding clients.

DID YOU KNOW?

During a typical examination, the Division reviews the compliance programs of RIAs in one or more of the following core areas: marketing practices, custody and safety of client assets, valuation, portfolio management, brokerage and execution, conflicts of interest, and related disclosures.

As in previous years, the Division prioritizes RIAs and registered funds that have never been examined, including recently registered firms, and those that have not been examined for a number of years. Typically, these examinations focus on firms' compliance programs.

B. Registered Investment Companies, Including Mutual Funds and ETFs

The Division will continue to prioritize examinations of registered investment companies, including mutual funds and ETFs, given their importance to retail investors. The Division typically reviews certain perennial focus areas during its assessments of registered funds' compliance programs and governance practices. Perennial areas include, among other topics, disclosures to investors, accuracy of reporting to the SEC, compliance with the

new rules and exemptive orders (including ETF rules and exemptive orders for non-transparent, actively managed ETFs, and custom baskets). As part of its review of registered funds' LRMPs, the Division will consider whether the programs are reasonably designed to assess and manage the funds' liquidity risk and review the implementation of required liquidity classifications, including firms' oversight of third party service providers.

Certain types of registered funds, portfolio investments, and fund practices will be prioritized. Examples of the types of funds include: (1) money market funds, which remain an important part of the registered fund industry to retail

and institutional investors for cash management and will be reviewed for compliance with applicable requirements, including stress-testing, website disclosures, and board oversight; and (2) business development companies, which will undergo reviews of their valuation practices, marketing activities, and conflicts of interest with underlying portfolio companies. The Division's focus on portfolio investments will include examinations of mutual funds investing in private funds to assess risk disclosure and valuation issues. EXAMS will also prioritize examinations of certain fund practices, including a focus on advisory fee waivers to assess the sustainability of services for firms that provide such waivers, and trading activities of portfolio managers that may be designed to inflate fund performance.

DID YOU KNOW?

Perennial areas include, among other topics, disclosures to investors, accuracy of reporting to the SEC, compliance with the new rules and exemptive orders (including ETF rules and exemptive orders for non-transparent, actively managed ETFs, and custom baskets).

III. BROKER-DEALER AND EXCHANGE EXAMINATION PROGRAM

A. Microcap, Municipal, Fixed Income, and Over-The-Counter Securities

The Division remains committed to deterring microcap fraud, or fraud in connection with securities of companies with a market capitalization under \$250 million. The Division will continue to prioritize examinations of broker-dealers for compliance with their obligations in the offer, sale, and distribution of microcap securities. Focus areas for examinations will include: (1) transfer agent handling of microcap distributions and share transfers; (2) broker-dealer sales practices and their consistency with Regulation BI; and (3) broker-dealer compliance with certain regulatory requirements, including the locate requirement of Regulation SHO, penny stock disclosure rules (*i.e.*, Rules 15g-2 through 15g-6 of the Securities Exchange Act of 1934 (Exchange Act)), and the obligation to monitor for and report suspicious activity and other anti-money laundering (AML) obligations.

States and local governments issue debt securities, referred to as municipal securities or municipal bonds, to finance a wide variety of public projects. Timely and accurate municipal issuer disclosure is vitally important to investors and the markets for these securities. The Division will examine the activities of broker-dealers, underwriters, and municipal advisors to assess whether these firms are meeting their respective obligations, as and to the extent applicable, in relation to municipal issuer disclosure.

In addition, the Division will examine broker-dealer trading activity in fixed income securities with a focus on sales practices; best execution obligations; fairness of pricing, mark-ups and mark-downs, and commissions; and confirmation disclosure requirements, including disclosures relating to mark-ups and mark-downs.

The Division's focus on products and services will also include the sale of over-the-counter securities and whether broker-dealers recommending these securities are meeting their obligations under Regulation BI. Examinations will also assess compliance with revised Exchange Act Rule 15c2-11, which generally requires broker-dealers to refrain from publishing quotations in a quotation medium for an issuer's security when current issuer information is not publicly available (among other requirements).

DID YOU KNOW?

The Division's focus on products and services will also include the sale of over-the-counter securities and whether broker-dealers recommending these securities are meeting their obligations under Regulation BI.

B. Broker-Dealer Operations

Broker-dealers that hold customer cash and securities have a responsibility to ensure that those assets are safeguarded in accordance with the Customer Protection Rule and the Net Capital Rule. Examinations of broker-dealers will continue to focus on compliance with these rules, including the adequacy of internal processes, procedures, and controls, and compliance with requirements for borrowing fully paid and excess margin securities from customers. Examiners may also assess broker-dealer funding and liquidity risk management practices to assess whether firms have sufficient liquidity to manage stress events.

The Division will continue to examine broker-dealer trading practices. Examinations will focus on broker-dealer compliance with best execution obligations in a zero commission environment and compliance with Exchange Act Rule 606 order routing disclosure rules. The Division will continue to review potential conflicts of interest in order routing, such as conflicts arising from payment for order flow, including wholesaler payments or exchange rebates, and the possible effect any conflicts of interest may have on order routing decisions and best execution obligations. Examinations will also focus on large trader reporting obligations and broker-dealer compliance with Regulation SHO, including the rules regarding aggregation units and locate requirements.

The Division will also examine the operations of certain alternative trading systems for compliance with Regulation ATS, and in particular focus on consistency with their disclosures provided in Form ATS-N.

As in previous years, EXAMS will prioritize the review of firms that are engaged in activities that appear to require broker-dealer registration and those that may be involved in the illegal distribution of unregistered securities to ensure investors are receiving the benefits of the federal securities laws.

C. National Securities Exchanges

National securities exchanges provide marketplaces for facilitating securities transactions and, under the federal securities laws, serve as self-regulatory organizations responsible for enforcing compliance by their members with the federal securities laws and rules and the exchanges' own rules. The Division will examine the national securities exchanges to assess whether they are meeting their obligations under the federal securities laws and will focus on exchange regulatory programs to detect and discipline violations, and participation in National Market System (NMS) Plans. Examinations may also assess and compare any exchange advisory services offered to issuers regarding ESG initiatives.

D. Security-Based Swap Dealers (SBSDs)

The compliance date for registration of SBSBs and several other SBSB requirements was October 6, 2021. Initial examinations of these new registrants will focus on the policies and procedures related to compliance with the security-based swap rules generally (*e.g.*, trade acknowledgement and verification, recordkeeping and reporting, and risk management requirements).

DID YOU KNOW?

The compliance date for registration of SBSBs and several other SBSB requirements was October 6, 2021.

E. Municipal Advisors

The Division will examine whether municipal advisors have met their fiduciary duty and conflict disclosure obligations to municipal entity clients. The Division will also examine whether municipal advisors have satisfied their registration, professional qualification, continuing education, and supervision requirements.

F. Transfer Agents

The Division will continue to examine transfer agents' core functions: the timely turnaround of items and transfers, recordkeeping and record retention, safeguarding of funds and securities, and filing obligations with the Commission. Examination candidates will include, among others, never-before-examined transfer agents and transfer agents that service microcap or municipal bond issuers, use novel technologies (*e.g.*, blockchain or online crowdfunding portal applications), or engage in significant paying agent activity.

IV. CLEARANCE AND SETTLEMENT EXAMINATION PROGRAM

The Division will conduct, as required by Title VIII of the Dodd-Frank Act, at least one risk-based examination of each clearing agency designated as systemically important and for which the SEC serves as the supervisory agency. These examinations will focus on core risks, processes, and controls and will cover the specific areas required by statute, including the nature of clearing agencies' operations and assessment of financial and operational risk. Additionally, the Division will conduct risk-based examinations of other registered clearing agencies which have not been designated as systemically important. The Division will also examine both groups of clearing agencies for compliance with the SEC's Standards for Covered Clearing Agencies, which are rules that require covered clearing agencies to, among other things, have policies and procedures that address maintaining sufficient financial resources, protecting against credit risks, managing member defaults, and managing operational and other risks.

In addition, EXAMS will conduct risk-based examinations of SEC-registered clearing agencies to: (1) determine whether their respective risk management frameworks comply with the Exchange Act, and serve the needs of their members and the markets they serve; (2) assess the adequacy and timeliness of their remediation of prior deficiencies, including, for example, the role of senior leadership in the remediation process; and (3) examine other risk areas identified in collaboration with the SEC's Division of Trading and Markets and other regulators. Areas of focus may include margin, counterparty credit risk, disclosure framework, governance, recovery and wind-down, default management, liquidity risk management, and project management, among other things.

V. REGULATION SYSTEMS COMPLIANCE AND INTEGRITY

The Commission adopted Regulation SCI to strengthen the technology infrastructure of the U.S. securities markets. Regulation SCI entities include national securities exchanges, registered and certain exempt clearing agencies, FINRA, MSRB, plan processors, and alternative trading systems that meet certain volume thresholds. Among other things, these critical market infrastructure entities must establish, maintain, and enforce written policies and procedures reasonably designed to ensure that their systems' capacity, integrity, resiliency, availability, and security is adequate to maintain their operational capability and promote the maintenance of fair and orderly markets.

EXAMS will continue to evaluate whether SCI entities have established, maintained, and enforced written policies and procedures as required. Areas of focus will include: (1) whether the incident response policies and procedures of SCI entities are reasonably designed, with a particular focus on ransomware; (2) the use of third-party network infrastructure services to support critical functions; (3) policies and procedures pertaining to the return to the workplace or further hybridization of the workplace after the extended telework posture caused by the COVID-19 pandemic; and (4) whether SCI entities have established reasonably designed policies and procedures to identify and mitigate software supply chain risks, including secure code development practices of SCI entities.

VI. FINRA

FINRA oversees approximately 3,400 brokerage firms, 153,000 branch offices, and 618,000 registered representatives through examinations, enforcement, and surveillance. In addition, FINRA, among other things, provides a forum for securities arbitration and mediation, conducts market regulation, including by contract for a majority of national securities exchanges, reviews broker-dealer advertisements, administers the testing and licensing of registered persons, and operates industry utilities such as Trade Reporting Facilities.

EXAMS conducts risk-based oversight examinations of FINRA. It selects areas within FINRA to examine through a risk assessment process designed to identify those aspects of FINRA's operations important to the protection of investors and market integrity, including FINRA's implementation of new investor protection initiatives. The analysis is informed by collecting and analyzing extensive information and data, regular meetings with key functional areas within FINRA, and outreach to various stakeholders, including broker-dealers and investor groups. Based on the outcome of this risk-assessment process, EXAMS conducts inspections of FINRA's major regulatory programs. EXAMS also conducts oversight examinations of FINRA's examinations of certain broker-dealers and municipal advisors. From its observations during all of these inspections and examinations, EXAMS makes detailed recommendations to improve FINRA's programs, its risk assessment processes, and its future examinations.

VII. MSRB

MSRB regulates the activities of broker-dealers that buy, sell, and underwrite municipal securities, as well as the activities of municipal advisors. MSRB establishes rules for municipal broker-dealers (including registered municipal securities dealers) and municipal advisors, supports market transparency by making municipal securities trade data and disclosure documents available, and conducts education and outreach regarding the municipal securities market. EXAMS, along with FINRA and the federal banking regulators, conducts examinations of registered firms to assess compliance with MSRB rules. EXAMS also applies a risk assessment process, similar to the one it uses to oversee FINRA, to identify areas to examine at MSRB. Examinations of MSRB evaluate the effectiveness of MSRB's policies, procedures, and controls.

VIII. THE LONDON INTER-BANK OFFERED RATE (LIBOR) TRANSITION

The discontinuation of LIBOR could have a significant impact on the financial markets and may present a material risk for certain market participants, including the RIAs, broker-dealers, investment companies, municipal advisors, transfer agents and clearing agencies overseen by the Division. Preparation for the transition away from LIBOR is essential for minimizing any potential adverse effects associated with LIBOR discontinuation. EXAMS will continue to engage with registrants through examinations and outreach efforts to assess their exposure to LIBOR and their transition to an alternative reference rate, preparations for the cessation of many LIBOR rates beginning immediately after December 31, 2021, and the transition to an alternative reference rate, in connection with registrants' own financial operations, the exposures of their clients and customers, and their obligations when recommending LIBOR-linked instruments.

IX. ANTI-MONEY LAUNDERING

The Bank Secrecy Act requires financial institutions, including broker-dealers and registered investment companies, to establish AML programs that are tailored to address the risks associated with the firm's location, size, and activities, including customers they serve, the type of products and services offered, and the means by which those products and services are offered. These programs must, among other things, include policies and procedures reasonably designed to identify and verify the identity of customers and beneficial owners of legal entity customers, perform customer due diligence (as required by the Customer Due Diligence rule), monitor for suspicious activity, and, where appropriate, file Suspicious Activity Reports (SARs) with the Financial Crimes Enforcement Network. SARs are used to detect and combat terrorist financing, public corruption, market manipulation, and a variety of other fraudulent behaviors.

Given the importance of these requirements, the Division will continue to prioritize examinations of broker-dealers and registered investment companies for compliance with their AML obligations in order to assess, among other things, whether firms have established appropriate customer identification programs and whether they are satisfying their SAR filing obligations, conducting due diligence on customers, complying with beneficial ownership requirements, and conducting robust and timely independent tests of their AML programs. The goal of these examinations is to evaluate whether broker-dealers and registered investment companies have adequate policies and procedures in place that are reasonably designed to identify suspicious activity and illegal money-laundering activities.

DID YOU KNOW?

The goal of AML examinations of broker-dealers and investment companies is to evaluate whether they have adequate policies and procedures in place that are reasonably designed to identify suspicious activity and illegal money-laundering activities.

X. CONCLUSION

These priorities reflect the Division's assessment of certain risks, issues, and policy matters arising from market and regulatory developments, information gathered from examinations, and other sources, including tips, complaints, and referrals, and coordination with other Divisions and Offices at the SEC as well as other regulators. While the Division will allocate significant resources to the examination issues described herein, it will also conduct examinations focused on and devote resources to new or emerging risks, products and services, market events, and investor concerns. The Division welcomes comments and suggestions regarding how it can better fulfill its mission to promote compliance, prevent fraud, identify and monitor risk, and inform SEC policy. Our contact information is available at <https://www.sec.gov/exams>. If you suspect or observe activity that may violate the federal securities laws or otherwise operates to harm investors, please notify SEC staff at <https://www.sec.gov/tcr>.



U.S. Securities and Exchange Commission

DIVISION OF EXAMINATIONS

Washington, DC