



NATIONAL EXAM PROGRAM

RISK ALERT

By the Office of Compliance Inspections and Examinations (OCIE)¹

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In this Alert:

Topic: Retirement-Targeted Industry Reviews and Examinations Initiative

Key Takeaways: NEP staff intends to focus on certain registered investment advisers and broker-dealers that provide services or sell investment products to retail investors. Examination focus areas include: reasonable basis for recommendations; conflicts of interest; supervision and compliance controls; and marketing and disclosure.

Retirement-Targeted Industry Reviews and Examinations Initiative

I. Introduction

Earlier this year, OCIE announced that its 2015 Examination Priorities includes a focus on “examining matters of importance to retail investors and investors saving for retirement.”² Consistent with this priority, OCIE is launching a multi-year Retirement-Targeted Industry Reviews and Examinations (ReTIRE) Initiative.

II. Background

Many retail investors, including advisory clients and brokerage customers, are more dependent than ever on their own investments for retirement.³ OCIE is focusing on retirement-based savings in recognition of the complex and evolving set of factors that retail investors face when making such investment decisions. Some of these factors include the broad and changing array of investments available

and services offered and the changing market environment. OCIE, through the National Examination Program (NEP), will conduct examinations of SEC-registered investment advisers and broker-dealers (collectively, registrants) under the ReTIRE Initiative that will focus on certain higher-risk areas of registrants’ sales, investment, and oversight processes, with particular emphasis on select areas where retail investors saving for retirement may be harmed.

¹ The views expressed herein are those of the staff of OCIE, in coordination with other staff of the Securities and Exchange Commission (SEC or Commission), including staff of the Division of Investment Management and the Division of Trading and Markets. The Commission has expressed no view on the contents of this Risk Alert. This document was prepared by the SEC staff and is not legal advice.

² OCIE, “[Examination Priorities for 2015](#)” (January 13, 2015).

³ See Pensions & Investments, “[Corporate retirement plans near tipping point – Defined contribution ascendency to transform how private plans do business](#)” (February 9, 2015). As of September 30, 2014, for the top 1,000 retirement plans surveyed, defined contribution (DC) pension plan assets exceeded defined benefit (DB) pension plan assets by \$284 billion. Under DC plans, individual investment accounts are established and often subsidized by employers, but are owned and controlled by employees. This contrasts with DB plans, which are pension plans that pay employees a lifetime annuity, often based on years of service and final salary.

III. Examinations

The staff intends to use data analytics, information from prior examinations, and examiner-driven due diligence to identify registrants to examine under this Initiative. As part of the examinations or the selection of examination candidates, the staff may focus on the activities of investment advisory representatives and/or broker-dealer registered representatives (collectively, representatives). The risk-based examinations conducted under the ReTIRE Initiative will focus on the services offered by the registrants to investors with retirement accounts in the following areas:

- **Reasonable Basis for Recommendations.** Registrants have important obligations under the federal securities laws and SRO rules (with respect to broker-dealers) when making recommendations or providing investment advice.⁴ To the extent applicable and required, the staff will assess the actions of registrants and their representatives for consistency with these obligations when: (i) selecting the type of account;⁵ (ii) performing due diligence on investment options; (iii) making initial investment recommendations; and (iv) providing on-going account management.
- **Conflicts of Interest.** Many registrants have inherent conflicts of interest that exist as a result of, among other things, their business structure, compensation structure, personal issues or relationships, or relationships with service providers. Generally, registrants may be expected, as applicable, to identify material conflicts of interest, to design compliance programs to address the risks caused by those conflicts,⁶ and/or to disclose material conflicts of interest.⁷ The staff will review registrants' sales and account selection practices in light of the fees charged, the services provided to investors, and the expenses of such services to evaluate, to the extent applicable and required, whether: (i)

⁴ See, e.g., [Status of Investment Advisory Programs under the Investment Company Act of 1940](#), Advisers Act Release No. 1623 (March 24, 1997) (discussing an investment adviser's duties to clients in the context of adopting a final rule providing for a non-exclusive safe harbor from the definition of investment company for certain investment advisory programs), [Registration Under the Advisers Act of Certain Hedge Fund Advisers](#), Advisers Act Release No. 2333 (December 2, 2004) (discussing the pertinent provisions of an adviser's "fiduciary" obligations); *Hanly v. SEC*, 415 F.2d 589, 596 (2d Cir. 1969); and [FINRA Rule 2111](#) (Suitability).

⁵ See FINRA, [Rollovers to Individual Retirement Accounts](#), Regulatory Notice 13-45 (December 2013) (FINRA Regulatory Notice 13-45) ("A recommendation concerning the type of retirement account in which a customer should hold his retirement investments typically involves a recommended securities transaction, and thus is subject to Rule 2111. For example, a firm may recommend that an investor sell his plan assets and roll over the cash proceeds into an IRA. Recommendations to sell securities in the plan or to purchase securities for a newly-opened IRA are subject to Rule 2111.").

⁶ See, e.g., [Compliance Programs of Investment Companies and Investment Advisers](#), Advisers Act Release No. 2204 (December 17, 2003) (Compliance Rule Adopting Release). See also Carlo DiFlorio, former Director, OCIE, "[Conflicts of Interest and Risk Governance](#)" (October 22, 2012); FINRA Regulatory Notice 13-45; and FINRA, [Report on Conflicts of Interest](#) (October 2013).

⁷ For a discussion of investment advisers' and broker-dealers' duties relating to disclosure of conflicts of interest, see generally Staff of the U.S. Securities and Exchange Commission, [Study on Investment Advisers and Broker-Dealers](#) (January 2011), at 22-24, 55-58.

compliance programs identify and address risks associated with the conflicts of interest and (ii) material conflicts of interest, such as compensation structures that may incentivize representatives to make certain recommendations, are disclosed or otherwise addressed.

- **Supervision and Compliance Controls.** Under applicable federal securities laws and SRO rules (for broker-dealers), registrants must reasonably supervise persons acting on their behalf and adopt effective compliance programs, which should include reasonably designed policies and procedures that are tailored to each firm's business.⁸ The staff will review registrants' controls, oversight, and supervisory policies and procedures, as appropriate, and for compliance with any applicable specific requirements discussed therein. In addition to these review areas, the staff may focus on: (i) registrants with operations in multiple and/or distant branch offices and (ii) representatives with outside business activities.
- **Marketing and Disclosure.** Registrants generally must ensure that materials distributed to investors are not deceptive or misleading.⁹ The staff will review registrants' brochures, sales and marketing materials, and disclosures to retail investors to, among other things, validate, to the extent applicable and required, that: (i) the content of the materials and representations of representatives are true and accurate and do not omit material information where there is a duty to disclose; (ii) disclosures regarding the fees are complete and accurate; and (iii) credentials or other endorsements are valid and meet any stipulated standards.

While these are the primary focus areas for the ReTIRE Initiative, examiners may select additional topics based on operational and other risks identified during the examinations.

IV. Conclusion

In sharing the focus areas for the ReTIRE Initiative, the NEP's intent is to encourage registrants to reflect upon their own practices, policies, and procedures in these areas and to promote improvements in their supervisory, oversight, and compliance programs, as deemed appropriate.

⁸ See [Exchange Act Sections 15\(b\)\(4\)\(E\) and 15\(b\)\(6\)\(A\)](#) and [Advisers Act Section 203\(e\)\(6\) and 203\(f\)](#), which authorize the Commission to take action against registrants and their associated persons for failure to supervise their personnel who violate the federal securities laws. See also [Advisers Act Rule 206\(4\)-7](#) (the Compliance Rule); Compliance Rule Adopting Release; and [FINRA Rules 3110](#) (Supervision), [3120](#) (Supervisory Control System), and [3130\(a\)](#) (Annual Certification of Compliance and Supervisory Processes).

⁹ See, e.g., [Advisers Act Sections 206\(1\), \(2\), and \(4\)](#), and [Rule 206\(4\)-1 thereunder](#); [Section 17\(a\) of the Securities Act of 1933](#); [Exchange Act Sections 10\(b\) and 15\(c\)](#) and [Rule 10b-5 thereunder](#); and [FINRA Rule 2210](#) (Communications with the Public).

This Risk Alert is intended to highlight for firms risks and issues that the staff has identified. In addition, this Risk Alert describes factors that firms may consider to (i) assess their supervisory, compliance and/or other risk management systems related to these risks, and (ii) make any changes, as may be appropriate, to address or strengthen such systems. These factors are not exhaustive, nor will they constitute a safe harbor. Other factors besides those described in this Risk Alert may be appropriate to consider, and some of the factors may not be applicable to a particular firm's business. While some of the factors discussed in this Risk Alert reflect existing regulatory requirements, they are not intended to alter such requirements. Moreover, future changes in laws or regulations may supersede some of the factors or issues raised here. The adequacy of supervisory, compliance and other risk management systems can be determined only with reference to the profile of each specific firm and other facts and circumstances.
