

[Securities Regulation Daily Wrap Up, INVESTMENT ADVISERS—SEC’s Compliance, Enforcement and IM Divisions discuss COVID-19-coping, \(Nov. 19, 2020\)](#)

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Division directors amazed by their staff’s extraordinary output during the pandemic and emphasize their successfully coordinated efforts.

Peter Driscoll, the SEC’s Compliance Inspections and Examinations Office (OCIE) Director opened the November 19, 2020 10th annual Compliance Outreach program (for Investment Adviser and Investment Adviser Senior Officers) by remarking upon the effects that COVID-19 has had on the Commission’s various Divisions, as well as the extraordinary remote work the Compliance Office, the Enforcement Division (led by Deputy Director Marc Berger) and the Investment Management (IM) Division (led by Director Dalia Blass) have [accomplished](#) during the pandemic.

OCIE. Director Driscoll began by remarking upon how well his staff stepped up from the mid-March 2020 start of the pandemic to remotely continue the OCIE’s mission with few disruptions. The OCIE’s highest priority, he said, has been staff’s health but that SEC technological advances have allowed them to continue to perform due diligence over investment adviser firms from their remote locations (home) while simultaneously staying healthy. He applauded staff for the following extraordinary work they accomplished in 2020 under extremely difficult circumstances: (1) conducting 2,950 examinations of firms collectively comprising \$4.9 million funds and \$3.4 trillion in assets under management; (2) addressing firm compliance with Regulation Best Interest and Form CRS; (3) remotely holding 300 outreach events; and (4) releasing eight risk alerts.

Driscoll next launched into a discussion of the chief compliance officer’s (CCO) role in an investment advisory firm. He proclaimed that the OCIE’s most recent risk alert provides guidance on this role but that a number of firms are not abiding by it and are, instead, faking the role. Driscoll remarked, however, that even OCIE examinations and inspections conducted remotely will reveal when a firm is giving only lip service to the CCO by, for example, having him or her check boxes on a compliance form without providing meaningful commentary. He specified that to be effective, a CCO must be given seniority by the firm that is accompanied by empowerment, authority and commensurate pay, to enable the CCO to make decisions ensuring that registrants comply with federal securities laws and regulations, as well as to allow the CCO a direct communication channel to the firm’s senior management or, better yet, be deemed a senior management member.

Driscoll emphasized, however, that the CCO’s role must not exist in a vacuum. He or she cannot be blamed for all the firm’s compliance mistakes. Instead, the CCO must have a partnership with the firm’s management so that both parties can address compliance issues together. Notwithstanding the above failures, Driscoll noted that many firms have complied with the risk alert’s guidance by having an empowered CCO. He also applauded firms for having business continuity plans in place that impliedly cover Covid-19 and cybersecurity disruptions. Lastly, Driscoll mentioned that firms periodically ask the OCIE such questions as "whom should the CCO report to in the firm?" or "how much should a firm budget for compliance?" Driscoll acknowledged that these questions are hard to answer and, moreover, add to a firm’s pandemic burden by having its staff work remotely and conduct meetings virtually while simultaneously juggling their personal responsibilities to family members during this difficult time.

Enforcement and IM pandemic responses. Deputy Director Berger. As the outreach program’s moderator, Driscoll then asked Enforcement Deputy Director Berger and Director Blass how their respective Divisions are

coping with COVID-19. Berger remarked that the Enforcement Division has been teleworking since mid-March but that the disruption has not prevented his staff from investigating or bringing 490 enforcement actions in 2020. More specifically, he said that the Division has been able to conduct remote testimony as well as hold both defense council and Wells meetings, and also render settlements. There has been a litigation lull, however, because of physical trial slow-downs, but he noted that this year saw the Division's first virtual trial in New York's Southern District Court and a four-day bench trial in Louisiana. In short, he said that the Enforcement Division has, overall, pivoted well during the pandemic.

Berger also emphasized the important partnerships that have successfully continued virtually during the pandemic between the enforcement and IM divisions, and the OCIE. He noted, for example, his reliance on the OCIE to converse with his staff on whether particular compliance inspections and examinations should become enforcement actions, along with the "critical interplay between his office and Dalia's" on whether certain defendants being investigated for possible enforcement action have violated either the 1940 Investment Company Act or the 1940 Investment Advisers Act.

Lastly, Berger discussed recent complex products being recommended to advisory clients, also touching on private funds and cybersecurity breaches. Regarding complex products, he noted recent Enforcement Division discussions about whether to bring enforcement actions against firms who recommend these products without disclosing the risks to their clients or without mentioning the conflicts of interest that might motivate advisers to recommend particular products. Berger similarly mentioned the conflict of interest in connection with managing client private funds, which is often at least 40 percent of the funds managed by approximately 13,800 advisory firms. And along with bringing enforcement actions for not disclosing these private fund conflicts of interest, Berger stated an increase in enforcement actions for investment adviser custody rule violations even when a violation has not led to the firm's misusing a client's funds or securities. On cybersecurity, Berger emphasized that an advisory firm's client data breach will not necessarily result in enforcement action against the firm, especially if the OCIE has taken a first look at the situation and determined that the occurrence was inadvertent rather than the firm's fault.

Director Blass. Director Blass's answers to the same questions asked Deputy Director Berger were as follows:

- Blass declared that like the Enforcement Division, the IM Division remained fully functional working remotely during the pandemic by, among other things, responding to hundreds of outreach calls from registrants, reaching out to staff in all SEC divisions who possess deep knowledge on particular topics the IM Division needed information about, and fine-tuning 65 regulatory/policy initiatives begun in 2017.
- Blass lauded the coordinated efforts that virtually occurred between the various Divisions, particularly remarking upon her staff's ability to perform their jobs because of the vast amount of data they were able to view from SEC technological advances, along with her ability to glean deep knowledge on important topics from experts across the Commission's Divisions.
- Regarding Berger's above-mentioned critical interplay between the OCIE, Enforcement and IM Divisions, Blass emphasized her ability to communicate with Driscoll and Berger when drafting a rule or policy to determine from them whether compliance with, and enforcement of, the rule or policy would actually be possible.
- On complex products, Blass acknowledged the possibility that investment advisers recommending these products might not appreciate the risks or rewards to communicate them to their clients, and furthermore that firms might not realize that these products, depending on whether they are exchange traded funds (ETFs), ETP, commodity pools or certain derivatives, are subject to the 1940 Act, the Advisers Act, Regulation Best Interest and/or the investment adviser fiduciary duty standard; she mentioned five SEC actions filed last week in connection with a risk based initiative she worked on involving the recent escalation of firms making bad, high risk product recommendations to retail clients.
- On cybersecurity, Blass declared that firms teleworking during the pandemic have increased their cybersecurity risks, and that they should reach out to the IM Division on what guidance the Division should publish on this issue.

- Going forward, Blass said that the IM Division will be tackling possible amendments to long-standing regulations on valuation, advertising/general solicitation, open-end funds, shareholder reports, investment adviser custody rules (particularly the intersection between custody and digital assets), and electronic delivery of documents (especially large documents) because of COVID-19's having rendered office printing and physical mailing of these documents an impossibility.

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