



Risk Management Update October 2009

DRAFT OF 2010-2015 SEC STRATEGIC PLAN PUBLISHED FOR COMMENT

The Securities and Exchange Commission (“SEC” or “Commission”) has released for comment of its much anticipated Strategic Plan for Fiscal Years 2010 to 2015 (the “Strategic Plan”).^[1] The Strategic Plan addresses many of the overall goals and outcomes sought by the SEC as a matter of principle and as a result of its congressional mandate to protect investors, promote fair and efficient markets, and facilitate capital growth. The broad goals outlined in the Strategic Plan include the familiar adages championed by the SEC since its inception: (1) foster and enforce compliance with the federal securities laws; (2) establish an effective regulatory environment; (3) facilitate investor access to information; and (4) enhance the Commission’s performance by maximizing its resources.^[2] But not surprisingly, there is a noticeable change in the Commission’s approach for the next five years outlined in the Strategic Plan.

It is no secret that the Commission is in the process of making significant, long-term changes to its regulatory and enforcement approach in the wake of the financial crisis that raised questions about the regulatory body’s effectiveness. On August 31, 2009, the SEC Office of Inspector General released its report entitled *Investigation of Failure of the SEC to Uncover Bernard Madoff’s Ponzi Scheme*, which identified numerous missed opportunities to uncover the fraudulent practices of Bernard Madoff.^[3] In response, the SEC’s Director of the Division of Enforcement and the Acting Director of the Office of Compliance Inspections and Examinations testified before the Senate Committee on Banking, Housing, and Urban Affairs and provided significant detail regarding the Commission’s efforts to step up its fraud detection and prevention practices.^[4] The Strategic Plan mirrors many of the initiatives detailed in the testimony, including advancing the expertise of SEC staff members, enhancing communication and coordination among various offices and divisions and with third parties, improving examination and investigative planning, and reallocating and expanding the resources available to SEC staff.

The Specifics of the Strategic Plan

At the outset, the Strategic Plan mentions the Commission’s role in the overall reforms occurring in the financial regulatory system as a whole, noting the need to improve inter-agency cooperation and communication as well as the potential legislation that would require managers of hedge funds and other private pools of capital to register with and be subject to SEC regulation.^[5] Much of the plan focuses on enhancing transparency and improving disclosure throughout the securities industry and details how the SEC is improving its oversight capabilities using lessons learned from the financial crisis. While it is foreshadowed that the SEC likely will take significant, unprecedented steps to address various perceived regulatory gaps, the current draft of the plan offers little insight

into specifics of any contemplated reforms. Nevertheless, a close read does provide a glimpse into those focus areas that the SEC may set its sights on for deploying more effective regulation through new initiatives and innovative strategies.

Foster Compliance with Securities Laws

To achieve its goal of fostering compliance with the securities laws, the SEC plans to more actively encourage those organizations it regulates to adopt a strong “culture of compliance.” To help foster this, the SEC plans to better communicate its findings from inspections and enhance its publication of major enforcement actions as a deterrent. Notably, the SEC claims to have several initiatives underway to improve its ability to detect violations of the securities laws. The agency is completely re-assessing its risk-based approach to examination of registrants and plans to substantially increase the number of cause and special examinations conducted through its use of a more robust risk assessment process focused on areas most susceptible to fraud or other major violations of the securities laws. Other outcomes sought include enhancing and expanding the SEC’s enforcement program through collaboration with other regulators and increasing the percentage of “high impact” cases successfully resolved.^[6]

Establish an Effective Regulatory Environment

The Commission has set forth several significant and noteworthy objectives with regard to establishing an effective regulatory environment. The Strategic Plan directs the SEC staff charged with drafting rules and regulations to ensure that they are clearly written, easily understood, and tailored toward specific ends, and to regularly review its rulemaking process to better achieve this objective. The Commission plans to commence a survey of broker-dealers and investment advisers to determine whether the Commission’s regulatory requirements are clear and will obtain suggestions and guidance on establishing a more understandable regulatory environment. The Strategic Plan also states that the SEC will seek to harmonize the regulatory systems that apply to broker-dealers and investment advisers.^[7] It remains unclear whether this means the establishment of a self-regulatory organization for registered investment advisers, or the expanded authority of FINRA to include oversight of SEC-registered investment advisers as well as broker-dealers. What is clear, however, is that the SEC actively is seeking to enhance its oversight of investment advisers and broker-dealers by requiring additional safeguards when firms have custody of client assets and mandating more meaningful disclosure of their business practices, conflicts of interests, and backgrounds.

Facilitate Investor Access to Information

The SEC believes that a critical component of effective regulation is ensuring that investors have sufficient access to information to permit them to make informed investment decisions. The first indication of the SEC’s investor education initiatives is the launching of www.investor.gov, the SEC’s new website designed to help investors protect their investments and avoid fraud.^[8] Similarly, as part of the SEC’s goal to facilitate investor’s access to information, the Strategic Plan indicates that the Commission intends to modernize disclosure requirements and amend the broker-dealer and investment adviser registration forms to better extract information that will help investors compare and select advisers and brokers. The Commission seeks to evaluate

investor interest in obtaining more information on broker-dealer compensation and conflicts of interests and expand the use of and access to the BrokerCheck and IAPD systems. The SEC believes that providing investors with greater availability of background information on broker-dealers and investment advisers will help facilitate better decision-making. It is unclear, however, the extent of the anticipated changes that will be made to these systems and the information that firms will be required to disclose.

Enhance the Commission's Performance

Finally, the Commission's goal of enhancing its performance and maximizing its resources includes greatly expanding internal training programs to expand staff expertise, and hiring programs designed to attract more economists, trading and investment specialists, and staff that have significant experience in fraud detection. The SEC seeks to acquire more staff with a status of Certified Fraud Examiner, Certified Financial Analyst, Series 7, or other relevant industry designations.^[9]

The SEC's Strategic Plan gives an insight into some of the goals and objectives the Commission sees as important in the years to come. The full text of the Draft Strategic Plan is available on the SEC's website at <http://www.sec.gov/about/secstratplan1015.pdf>. The SEC is seeking comments on the draft, which can be sent to strategicplan@sec.gov.

For more information, or to learn about how CCLS may be of assistance, please do not hesitate to contact us at (619) 278-0020.

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^[1] U.S. Sec. & Exch. Comm'n, Strategic Plan for Fiscal Years 2010-2015: Draft for Comment (2009), available at <http://www.sec.gov/about/secstratplan1015.pdf> [hereinafter Draft Strategic Plan].

^[2] *Id.* at 4.

^[3] Office of the Inspector Gen., U.S. Sec. & Exch. Comm'n, Report No. OIG-509, Investigation of Failure of the SEC to Uncover Bernard Madoff's Ponzi Scheme 41, (Aug. 31, 2009) available at <http://www.sec.gov/news/studies/2009/oig-509.pdf>.

^[4] Robert Khuzami & John Walsh, Testimony Concerning the SEC's Failure to Identify the Bernard L. Madoff Ponzi Scheme and How to Improve SEC Performance (Sept. 10, 2009), <http://www.sec.gov/news/testimony/2009/ts091009rk-jw.htm>.

^[5] Draft Strategic Plan, *supra* note 1, at 6-7. Such reforms have been called for by the Obama Administration, members of Congress, and the Treasury Department. See U.S. Department of the Treasury, Financial Regulatory Reform: A New Foundation 37-38 (2009) available at http://www.financialstability.gov/docs/regs/FinalReport_web.pdf. Some of the recent legislative proposals

that would require registration of managers of private investment vehicles include the Hedge Fund Transparency Act of 2009, the Hedge Fund Adviser Registration Act of 2009, the Private Fund Transparency Act of 2009, the Private Fund Investment Advisers Registration Act of 2009, and the Investor Protection Act of 2009.

^[6] The Strategic Plan describes “high impact” cases as those that are the first of their kind, those that achieve an appropriate deterrent effect, or those that are of particular importance to market participants or the public at large. Draft Strategic Plan, *supra* note 1, at 21. A case is considered successfully resolved when it “results in a favorable outcome for the SEC, including through litigation, a settlement, or the issuance of a default judgment.” *Id.* at 17.

^[7] *Id.* at 23.

^[8] The new website has information on investing wisely, avoiding fraud, and allows investors to ask the SEC questions or report suspicious activity.

^[9] Draft Strategic Plan, *supra* note 1, at 44.