

**Insights**

## **SEC DIVISION OF EXAMINATIONS PUBLISHES 2025 EXAMINATION PRIORITIES**

Oct 29, 2024

On October 21, 2024, the Division of Examinations (the “Division”) of the U.S. Securities and Exchange Commission (the “SEC”) published its annual Examination Priorities for 2025 (the “Exam Priorities”).

Below is a discussion of the Exam Priorities for investment advisers, registered investment companies, broker-dealers, self-regulatory organizations, and other market participants.

### **INVESTMENT ADVISERS**

The Division will continue to focus on whether investment advice offered to clients satisfies an adviser’s fiduciary obligations, and in particular, recommendations related to: (1) high-cost products; (2) unconventional instruments; (3) illiquid and difficult to-value assets; and (4) assets sensitive to higher interest rates or changing marking conditions, including commercial real estate.

The Division will also focus on dual registrants and advisers with affiliated broker-dealers, commonly focusing on:

1. assessing investment advice and recommendations regarding certain products to determine whether they are suitable for clients’ advisory accounts;
2. reviewing disclosures to clients regarding the capacity in which recommendations are made;
3. reviewing the appropriateness of account selection practices, including rollovers from an existing brokerage account to an advisory account; and
4. assessing whether and how advisers adequately mitigate and fairly disclose conflicts of interest.

Examinations will also continue to assess the effectiveness of advisers’ compliance programs and evaluate their core areas, which include marketing, valuation, trading, portfolio management, disclosure and filings, and custody. Advisers’ annual review of the effectiveness of their compliance programs are critical. The Division will continue to focus on whether compliance programs address

compliance with the Investment Advisers Act of 1940, as amended, and are reasonably designed to prevent advisers from prioritizing their interests over their clients' interests.

The Division acknowledges that private fund advisers remain a significant portion of the SEC-registered investment adviser population, and as such will continue to prioritize specific topics, such as:

1. the consistency of disclosures with actual practices and whether a private fund is exposed to market volatility and interest rate fluctuations, including strategies involving commercial real estate, illiquid assets, and private credit;
2. the accuracy of calculations and allocations of private fund fees and expenses;
3. disclosure of conflicts of interest and risks, and the adequacy of policies and procedures; and
4. compliance with new SEC rules, including Form PF amendments and updated marketing rules.

## **INVESTMENT COMPANIES**

The Division will continue to prioritize examination of registered investment companies that have never before been examined and those that have not been recently examined with particular focus on newly formed funds.

Examinations of registered investment companies will review their compliance programs, disclosures, and governance practices. Specific topics are likely to include: (1) fund fees and expenses, and any associated waivers and reimbursements; (2) oversight of service providers; (3) portfolio management practices and disclosures; and (4) issues associated with market volatility.

## **BROKER-DEALERS**

Exam Priorities included four focus areas for broker-dealers:

1. Regulation Best Interest ("Regulation BI")<sup>[1]</sup>;
2. Form CRS, the customer relationship summary;
3. Broker-dealer financial responsibility rules; and
4. Broker-dealer trading-related practices and services.

With respect to Regulation BI, examinations will focus on the following broker-dealer practices: (1) recommendations with regards to products, investment strategies, and account types and whether the broker has a reasonable belief that the recommendation is in the customer's best interest; (2) disclosures made to investors regarding conflicts of interest; (3) conflict identification and mitigation and elimination practices; (4) processes for reviewing reasonably available alternatives;

and (5) factors considered in light of the investor’s investment profile such as investment goals and account characteristics. Examinations will focus in particular on recommended products that are complex, illiquid, or present higher risk to investors.

Examinations will review the way a broker-dealer’s relationship summary describes the relationships and services it offers to retail customers, its fees and costs, and its conflicts of interest. They will also focus on compliance with the net capital rule, accounting practices, and operational resiliency programs.

With regard to trading-related practices and services, equity and fixed income trading practices remain a Division priority, in particular the structure, marketing, fees, and potential conflicts. The Division is also concerned with trading in pre-IPO companies and the sale of private company shares in secondary markets, as well as retail orders.

## **SELF-REGULATORY ORGANIZATIONS**

National securities exchanges, the Financial Industry Regulatory Authority (“FINRA”) and the Municipal Securities Rulemaking Board (“MSRB”) are also subject to examination by the Division.

With regards to exchanges the Division will examine whether they are complying with their own rules as well as securities laws, and examinations may take a deeper look at exchange governance, regulatory programs, and participating in National Market System Plans.

The Division selects major regulatory areas within FINRA to examine through a risk-assessment process, which is informed by collecting and analyzing extensive data, holding regular meetings with FINRA key functional areas, and reaching out to stakeholders such as broker-dealers and investor groups. The Division, along with FINRA and federal banking regulators, examines registrants to ensure compliance with MSRB rules and uses a risk-assessment process similar to that it uses to oversee FINRA to identify areas to examine at the MSRB.

## **OTHER MARKET PARTICIPANTS**

The Division will also examine other market participants in 2025, including municipal advisors, transfer agents, security-based swap dealers, security-based swap execution facilities, and funding portals.

The Division will continue to examine whether municipal advisors have met their fiduciary duty, whether they have complied with MSRB Rule G-42, which establishes standards of conduct and duties applicable to non-solicitor municipal advisors, and whether they have made required filings with the SEC.

The Division will continue to examine transfer agent processing of items and transfers, recordkeeping, safeguarding of funds and securities, and SEC filings.

Examinations will continue to focus on whether security-based swap dealers have implemented policies and procedures related to rule compliance, including whether they are meeting their obligations under Regulation SBSR<sup>(iii)</sup> to accurately report swap transactions to data repositories.

On November 2, 2023, the SEC adopted Regulation SE under the Exchange Act, which implements new rules and forms for securities-based swap execution facilities. As such, the Division may begin conducting examinations of registered securities-based swap execution facilities in late fiscal year 2025.

Finally, the Division will examine whether funding portals are making and preserving required records and records related to issuers who offer and sell, or attempt to offer and sell, securities through the funding portal. Examinations will also consider whether funding portals have proper compliance policies and procedures in place, such as those that prevent them from: (1) offering investment advice; (2) soliciting transactions in the securities displayed on the funding portal's platform; (3) compensating persons for such solicitation or based on the sale of securities displayed on the platform; and (4) holding, managing, possessing, or handling investor funds or securities.

## **RISK AREAS IMPACTING VARIOUS MARKET PARTICIPANTS**

The Division's focus on cybersecurity practices remains vital to safeguarding customer records and information, and particular attention will be on firms' policies, procedures, governance practices, data loss prevention, access controls, account management, and response to cyber-related incidents. With respect to third-party products and services in particular, the Division will consider risks and goals associated with third-party products, sub-contractors, services, and any information technology used by the business without the IT department's approval, knowledge or oversight, or non-supported infrastructure.

Examinations will also assess compliance with Regulations S-ID and S-P, in particular as firms' policies and procedures pertain to safeguarding customer records and information at firms providing electronic investment services. Examinations will consider identification and detection to prevent and protect against customer identity theft, firms' practices to prevent account intrusions, and firm training on identity theft prevention and whether policies and procedures are reasonably designed to protect customer records.

The Division remains focused on automated investment tools, AI, and trading algorithms or platforms, and the Division will, in particular, examine firms employing certain digital engagement practices, such as digital investment advisory services, recommendations, and related tools and methods. The Division will also assess how firms monitor and/or supervise their use of AI and the integration of regulatory technology to automate internal processes and optimize efficiencies.

The Division will, when appropriate, conduct examinations of registrants offering crypto asset-related services and whether the registrants: (1) meet and follow their codes of conduct when recommending or advising on crypto assets; and (2) routinely review, update and enhance their compliance practices, risk disclosures, and operational resiliency practices, if required.

The Division will also conduct examinations of Systems Compliance and Integrity (“SCI”) entities, which will focus on:

1. the policies and procedures regarding the operational, business continuity planning and testing practices of SCI entities;
2. the effectiveness of incident response plans; and
3. the policies and procedures pertaining to the security operations management tools employed by SCI entities to ensure that their SCI systems and indirect SCI systems have adequate levels of security.

Finally, anti-money laundering programs must, among other things, include policies, procedures, and internal controls reasonably designed to achieve compliance with the Bank Secrecy Act. Examinations will review whether broker-dealers and certain registered investment companies are appropriately tailoring their programs to their business model and its risks, conducting independent testing, establishing an adequate customer identification program, and meeting their Suspicious Activity Report filing obligations.

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[i] Rule 15l-1 under the Securities Exchange Act of 1934, as amended (the “Exchange Act”)

[ii] 17 CFR § 242 of the Exchange Act.

## **RELATED PRACTICE AREAS**

- Corporate

## MEET THE TEAM



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