



## Examinations

# The SEC Is Calling: What CCOs Should Expect During Initial Communications With OCIE Examiners (Part One of Two)

Sep. 13, 2018

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SEC examiners begin many routine examinations of private fund managers with lengthy calls with the adviser's chief compliance officer (CCO). In part designed to help the SEC obtain the greatest return on the investment of its limited resources, these calls provide SEC examiners with an opportunity to learn more about the relevant adviser's business and compliance program earlier in the exam process.

This two-part series examines the format and substance of these initial calls and provides guidance on how CCOs can prepare for these interactions with the examiners. This first article discusses the ways in which the SEC initiates the examination process and provides insight into the form and substance of these introductory calls between the examiners and the CCO, including who participates in them on behalf of each of the SEC and the adviser. The [second article](#) will examine how the SEC is using these calls to meet multiple objectives; outline the topics that are generally discussed during them; and explore how a CCO can prepare accordingly, including what documents and information he or she should review in advance and what materials should be on hand during these calls.

See "[Effects of Expanding SEC Investment Adviser Examinations](#)" (Mar. 24, 2016); and our three-part series "What Do Hedge Fund Managers Need to Know to Prepare for, Handle and Survive SEC Examinations?": [Part One](#) (Feb. 3, 2011); [Part Two](#) (Feb. 10, 2011); and [Part Three](#) (Feb. 18, 2011).

## How OCIE Initiates the Exam Process

### Initial Call With OCIE Staff

"In most examinations conducted by the SEC's Office of Compliance Inspections and Examinations (OCIE), a member of the OCIE staff will call the adviser's CCO to let him or her know that the adviser has been selected for an examination," explained [Joel Wattenbarger](#), partner at Ropes & Gray. The OCIE staff member placing that call tends to be the main point of contact for the adviser during the examination.

Although the SEC typically initiates the exam process by telephoning the CCO, "occasionally the SEC will send a message to the CCO through one of its secure communication systems, alerting the adviser to the examination," added ACA Compliance Group senior principal consultant [Molly Yakubian](#).

See our two-part series on understanding the SEC's national exam program: "[How OCIE Selects Advisers to Examine](#)" (Jul. 12, 2018); and "[Recent Exam Trends and How Fund Managers Can Determine the Type of Exam OCIE Is Conducting](#)" (Jul. 19, 2018).

These initial calls provide the SEC with an opportunity to address key aspects of the examination, including the initial document request list and the onsite portion of the examination. In terms of the initial request list, OCIE examiners typically let the CCO know that they plan to send that document in the "near future," which in practice is frequently later that same day or the next day, noted Wattenbarger.

The conversation regarding the onsite portion of the examination typically proceeds in one of two ways, Yakubian explained. In some instances, the OCIE staff member placing the call notifies the CCO when the examiners plan to visit the adviser's office to conduct the onsite portion of the exam. Alternatively, she has also observed OCIE inquire into the adviser's availability for the onsite portion of the exam.

The CCO of a global alternative investment manager confirmed that this was consistent with his experience when his firm underwent a routine exam. "During the initial call, OCIE notified me that the adviser had been selected for an examination, told me when the examiners planned to come onsite and advised me of when I should expect to receive the initial request list."

While each exam progresses down its own path, it appears that in many cases the substance of these initial calls is largely administrative and logistical in nature, and they last 15-30 minutes on average. Generally speaking, OCIE staff typically avoid engaging the CCO on substantive matters at this point in time, Wattenbarger explained.

CCOs have received initial calls from OCIE examiners that have steered away from the more ministerial approach, however. According to Yakubian, while it is somewhat rare, "we have observed exams where the SEC engaged the CCO on substantive matters about the adviser's business during the initial call." OCIE is more likely to take this approach with advisers that have been examined before, or in circumstances where it is fairly evident that the SEC is conducting a risk-based examination, she noted.

"When I was first contacted by OCIE regarding an examination, the OCIE examiner did ask some substantive questions about the adviser during the initial call," explained Adam J. Reback, partner and CCO at J. Goldman & Co., L.P. While the call was not a deep dive into the adviser's business, he continued, questions from the exam team touched on a number of topics, including:

- adviser's investment strategy;
- number of employees;
- background and experience of the CCO;
- structure of the adviser's compliance department;
- structure of the adviser and its affiliates; and
- number of funds managed by the adviser.

These initial calls from OCIE tend to catch many CCOs by surprise, Reback explained; "nevertheless, the examiners likely expect the CCO to have answers to high-level questions about the adviser's business." One way that CCOs can ensure that they remain prepared to respond to questions from the SEC is to keep on hand current, high-level information regarding the adviser and its business. For example, the CCO could keep a current copy of the adviser's due diligence questionnaire (DDQ) – provided it is updated on a regular basis – on his or her desk. "Another option would be for the CCO to create a cheat sheet of sorts that includes specific adviser-related data that the SEC may ask about," suggested Reback.

Although the agenda for the initial call from OCIE tends to be dictated by the SEC, “CCOs can also use this interaction as an opportunity to gather information about the examination,” explained **Brendan Kalb**, partner at Morgan Lewis and former general counsel and managing director at AQR Capital Management. “For example, when discussing the dates for the onsite portion of the exam, the CCO could ask the OCIE examiner ‘Do you know whom you would like to meet with while you are onsite?’” Obtaining this information not only ensures that the adviser will have the appropriate personnel available that day to meet with the SEC, but it will also help the CCO decide whom to prioritize when it comes to preparing individuals for interviews with the SEC. Kalb also suggested that the CCO ask OCIE how many individuals from the SEC will be coming onsite to the adviser’s office. That way, the adviser can prepare adequate space for the exam team.

“In my experience, the actual onsite portion of the examination will not commence until a few weeks after the adviser is notified of the examination,” Kalb added.

During the period of time between receiving the initial call from OCIE and the SEC conducting the onsite portion of the exam, the CCO should not only prepare him or herself for the exam, but perhaps more importantly, should use this time as an opportunity to prepare the adviser’s senior management and staff for the exam. This includes “explaining the examination process to the adviser’s employees, putting individuals on notice that they may be interviewed by the SEC during the examination and setting forth the adviser’s expectations for how individuals should behave when interacting with the SEC during the onsite portion of the exam,” Kalb explained.

## **Interim Call With OCIE Staff**

It is becoming increasingly common for OCIE examiners to also use this initial call as an opportunity to schedule an additional call (Interim Call) with the CCO – and possibly other members of the adviser’s senior management – to discuss more substantive matters regarding the adviser’s business. Interim Calls occur after the initial call from OCIE notifying the CCO that an examination of the adviser has been commenced but prior to OCIE conducting the onsite portion of the exam.

“For routine exams, we see OCIE requesting this Interim Call with the adviser in almost every instance,” explained Wattenbarger. “There may be some regional differences with respect to this practice, but in my experience, this now occurs in the vast majority of exams,” he continued. In terms of timing, individuals that have participated in these Interim Calls have reported that they can last from roughly 30 minutes to several hours.

Seward & Kissel counsel **David Tang** agreed that Interim Calls are becoming a fairly standard part of the routine exam process, but he was careful to distinguish these Interim Calls that take place in routine exams from the calls requested by the SEC in correspondence-type exams and exams of newly registered advisers. In the latter instances, OCIE does not plan to come onsite, although it reserves the right to do so, and all correspondence is conducted over the phone or in writing, leading to longer conference calls – two to three hours in some cases – and more detailed discussions.

See our two-part series on SEC remote examinations: “**What Hedge Fund Managers Can Expect**” (May 12, 2016); and “**How Hedge Fund Managers Can Prepare**” (May 19, 2016).

The timing of Interim Calls can vary. OCIE may request one before sending the adviser its initial request list. “In these cases, my sense is that OCIE likely has a good idea of the types of documents it plans to request, and it may use the Interim Call to learn more information in order to determine if the scope of the request, as well as the documents being requested, are

appropriately tailored,” noted **Todd Kaplan**, founder of Cloudbreak Compliance Group. In other cases, OCIE will have already sent the adviser its initial document request list, and the adviser may have already completed its first document production to the SEC.

“In my experience, the nature of the Interim Call is fairly substantive,” explained Wattenbarger. “When we first began to see this practice emerge, CCOs may have been unprepared for these Interim Calls, believing that they would be more administrative or logistical in nature,” he continued. Today, however, CCOs are better prepared for these calls and know what to expect.

“Some CCOs are reluctant to engage with the examiners beyond the absolute bare minimum,” Wattenbarger continued. “I recommend, however, particularly when the SEC is requesting an Interim Call, that the CCO respectfully ask the SEC examiners what they would like to discuss during the call and whether the CCO should include individuals that manage other functional areas within the adviser,” he noted.

CCOs can also use these calls to present the adviser to the SEC in the best light possible, suggested Wattenbarger. Because these calls occur early on in the examination, it is likely that the OCIE examiners possess a limited amount of information about the adviser. Therefore, these calls provide the CCO with an opportunity to explain, in his or her own words, “the adviser’s business; how the adviser makes money for its clients; and the ways in which the firm handles operational and compliance issues,” he noted. In essence, “these calls give the adviser the ability to plan ahead, put its best foot forward and educate the exam staff about its business.”

## Who Participates in the Interim Call

The individuals that are most likely to take part in the Interim Call on behalf of the SEC are the members of the exam team; any other staffers that may be present during the exam; and the branch chief or his or her designee, Kalb explained. “The SEC uses these calls to introduce the exam team to the CCO, and in turn, the CCO is introducing the adviser to the exam team,” Reback noted.

Regarding the individuals from the adviser that are generally present on the call, “the SEC expects the CCO to be on the call, and then in many cases the examiners will leave it up to the adviser as to whether anyone else joins the call,” Tang explained. Therefore, CCOs should consider whether including other members of senior management – such as the portfolio manager, chief operating officer or chief financial officer – would add value to the call.

Some CCOs prefer to handle these calls on their own, however. Reback noted, “as the CCO and point person during the exam, I decided to handle both the initial call and Interim Call with the SEC on my own.” He pointed out, however, that he took a different approach once the OCIE examiners came onsite. “We kicked off our initial onsite meeting with the OCIE examiners with a first-day presentation, during which I walked the examiners through the specifics of the adviser’s business.” Reback explained that he included other members of senior management in that meeting in case the SEC had questions about the portion of the presentation for which those individuals were responsible.

The CCO of a global alternative investment manager added that, unless the SEC specifically requests to speak with a member of business team during the Interim Call, he would probably not include those individuals at this stage of the exam. On the other hand, “if a separate person serves as the adviser’s general counsel (GC), it likely makes sense for the CCO and GC to field initial questions from the OCIE examiners, as most of those questions will concern compliance, governance and structural matters,” he added.

The general consensus among those with whom the Hedge Fund Law Report spoke for this article series was that, in most cases, advisers should not include outside counsel on these Interim Calls. According to Tang, “outside counsel is generally advising in the background during a routine exam.” He added that although he does not typically take part in the Interim Call, he does prepare his clients for it, and clients brief him after the fact on what transpired during that call.

When it comes to whether an adviser’s compliance consultants should join the Interim Call, the approach among practitioners was less absolute. Tang noted that “although the adviser may be outsourcing certain aspects of its compliance program, the adviser and its CCO still need to own the compliance program.” Consequently, he explained that in many cases, compliance consultants should not be part of this call in order to avoid the appearance that the adviser is overreliant on its consultants.

On the other hand, while acknowledging a clear preference for the CCO to be able to answer the SEC’s questions, “if the consultants perform a lot of the heavy lifting for the adviser, they may need to be on the call,” noted the CCO of a global alternative investment manager. This is more likely to be the case at smaller advisers where individuals are wearing multiple hats, and the CCO may need more support, Kalb added. The risk of having compliance consultants join the call is that it may draw additional scrutiny of the adviser’s compliance program in light of the SEC’s focus on outsourced CCOs.

See our two-part series on the SEC’s risk alert about outsourced CCOs: “[Why All Investment Advisers – and Their Compliance Officers – Should Heed](#)” (Mar. 3, 2016); and “[Steps All Investment Advisers – and Their Compliance Officers – Should Take in Light Of](#)” (Mar. 10, 2016).

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