

The background features a dark blue and teal color palette with various financial data visualizations. On the left, there is a bar chart with several vertical bars of varying heights. In the center and right, there are line graphs with multiple colored lines (red, orange, green) and a prominent red triangle pointing downwards. Vertical columns of binary code (0s and 1s) are scattered throughout the background, adding a digital or data-driven aesthetic.

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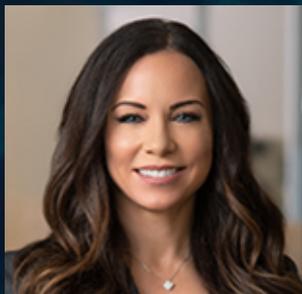
IMPACT OF SEC'S EXPANDED INVESTIGATIONS INTO OFF- PLATFORM MESSAGING

March 2, 2023

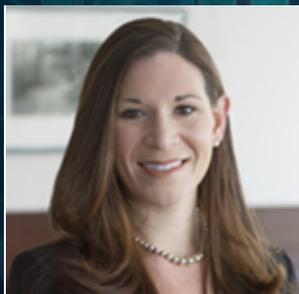
Presenters



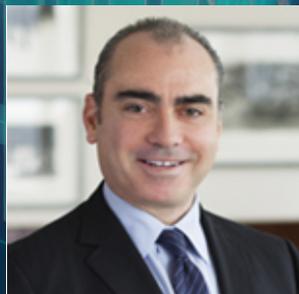
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Private Funds Landscape Overview

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How Did We Get Here?

Increased SEC Focus on Private Fund Managers

2015



OCIE Private Funds Unit formed

2017



Examination Priorities: One sentence on last page about "private funds"

2018



Examination Priorities: One sentence concerning "private fund advisers that manage funds with a high concentration of investors investing for the benefit of retail clients, including non-profit organizations and pension plans"

2020



Examination Priorities: Small section with focus on "RIAs to private funds that have a greater impact on retail investors"

June 23, 2020

Risk Alert:
"Observations from Examinations of Investment Advisers Managing Private Funds"

2022



Examination Priorities: Listed as first "Significant Focus Area"

2023



Examination Priorities: "In the past five years, there has been an 80% increase in the gross assets of private funds, with retirement plans steadily contributing to this growth."

How Does This Issue Arise?

Enforcement Investigations

- Direct from enforcement sweeps
- Investor complaints
- Unrelated products and services
- Unrelated events such as cyberattacks

Examinations: 2023 Priorities

- RIAs to Private Funds are a “Notable New and Significant Focus Area”
- RIA Examinations: “Examinations will review RIA policies and procedures for retaining and monitoring electronic communications”
- Never Before Examined RIAs: “As in previous years, the Division prioritizes RIAs that have never been examined, including recently registered firms, and those that have not been examined for a number of years”

SEC Investigations of Business Communications via Personal Messaging Platforms

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Initial Broker-Dealer Probe into Off-Channel Communications

- In September 2022, the SEC fined 16 financial firms a combined **\$1.8 billion** for failing to monitor and preserve business communications made on employees' personal devices and apps such as WhatsApp, in violation of federal securities laws.
- The SEC investigation uncovered "pervasive off-channel communications" by employees at multiple levels of authority.
 - The SEC issued a statement noting that, "as technology changes, it's even more important that registrants appropriately conduct their communications about business matters within only official channels, and they must maintain and preserve those channels."
 - Describing recordkeeping requirements as "sacrosanct," the SEC urged broker-dealers and asset managers subject to the federal securities laws to "self-report and self-remediate any deficiencies."

Initial Broker-Dealer Probe into Off-Channel Communications

- The SEC conducted its investigation by requesting the review of communications from personal devices of junior and senior bankers and traders at the firms, finding violations at all levels.
 - The probe found examples of employees talking often about “business matters” through texts on personal devices.
- In addition to the significant penalties, the firms:
 - Admitted wrongdoing;
 - Were ordered to cease and desist from future violations of the relevant recordkeeping provisions and were censured; and
 - Agreed to retain compliance consultants to conduct a comprehensive **review of policies and procedures** related to retention of electronic communications on personal devices and for **addressing noncompliance** by employees.

Expansion in Scope to Investment Funds and Advisors

- The SEC thereafter broadened the probe to include investment advisers and major hedge fund and private equity firms, several of which disclosed the inquiries in quarterly filings.
- Multiple firms were contacted by the SEC in October 2022 to provide information and documents related to their record-retention policies for certain types of “off-channel” electronic business communications, including text messages and messages on WhatsApp, WeChat, and similar applications.

Recent Inquiries

Requests have expanded to seeking information on:

- Details about reviews of policies and procedures, including those who are responsible for overseeing them; training programs; disciplinary action; and remediation efforts
- Documentation of how firms' organizations are set up, including information about individuals in each business unit who are responsible for communicating with investors

Regulatory Requirements & Objections to Scope of SEC Inquiries

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Investment Advisers Act of 1940

- **Rule 204-2(a)(7)** requires investment advisers to keep originals of all written communications received and copies of all written communications relating to:
 - (i) Any recommendations or advice provided;
 - (ii) Receipt, disbursement, or delivery of funds or securities;
 - (iii) The placement or execution of any order to purchase or sell any security; and
 - (iv) Performance of any and all managed accounts.

Investment Advisers Act of 1940

- **Rule 204-2(e)(1)** requires investment advisers to preserve communications in an easily accessible locations for at least five years.
- **Rule 206(4)-7** requires investment advisers to:
 - (i) Adopt and implement written policies and procedures to ensure compliance with the Investment Advisers Act;
 - (ii) Review these policies and procedures for adequacy and effectiveness on at least an annual basis and;
 - (iii) Designate a supervised chief compliance officer who is responsible for administering these policies and procedures.

Objections to the Scope of SEC Inquiries

- On January 31, 2023, trade associations, including the Managed Funds Association (MFA) and SIFMA, sent a letter to the SEC Chair Gary Gensler objecting that the Commission's investigation implicates serious privacy concerns and raised questions regarding the scope and application of the recordkeeping provisions of the Investment Advisers Act.
- The letter argues that:
 - The Investment Advisers Act's recordkeeping requirements are narrower than those applicable to broker-dealers under the Securities Exchange Act of 1934 because the Investment Advisers Act enumerates certain categories of communications required to be retained, whereas the Exchange Act has no similar limitations and reflects broader catch-all language.
 - The SEC itself has previously recognized that there are differences in books-and-records requirements applicable to broker dealers and investment advisers.

Objections to the Scope of SEC Inquiries

- The letter also urged the SEC to avoid equating employee noncompliance with policies regarding retention with firm violations.
 - Many firms' policies already require employees to only use approved channels for communications; penalizing firms for noncompliance is unfair and overbroad.
- Finally, the letter also objected to the SEC's request for review of personal devices as "extremely invasive," including because it would lead to collection of sensitive personal information unrelated to business communications such as medical information and passwords.
 - It pointed to potential violations of stringent international privacy requirements, including the EU's General Data Protection Regulation (GDRP).
- The MFA letter requested formal guidance including a notice-and-comment process.

Best Practices & Key Policies

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Key Policies to Implement and/or Review

- Record-retention policies should be reviewed to ensure compliance with SEC rules. Policies should also include sufficient enforcement mechanisms and appropriate disciplinary procedures.
- Firm policies should remind employees not to conduct business on WhatsApp or Facebook Messenger, or through personal text-messaging and email that are not retained.
- Conduct recurring training on record-retention and communication policies and consider requiring employees to attest monthly or quarterly that they are in compliance.
- Policies should inform employees that personal devices used to conduct company business are subject to monitoring and search.
 - An amendment to New York law effective May 2022 requires all employers to provide employees with and post publicly written notice that emails, phone calls, and other electronic communications can be monitored.

Key Policies to Implement and/or Review

Remote-work policies

- Monitoring of employee communications, including on work and personal devices, took on new challenges during the COVID pandemic, some of which remain as certain employee populations continue to work remotely some or all of the time.
- Employees, as well as clients, may have become accustomed to speaking through texts or apps that are viewed as convenient and quick.
- Remote-work policies should reinforce that employees may not communicate via unauthorized channels, that communications must be retained, and that employee communications are subject to monitoring.
- Training should include information on how to navigate client communication-preference issues (both when working remotely and in the office).

Whistleblower/reporting policies

- The SEC has also been focused recently on preventing companies from using confidentiality and other policies to deter reporting to the SEC.
- Firms should be mindful of this enforcement priority as they communicate with employees and develop and enforce policies, including policies regarding reporting of potential retention and off-channel communication violations.
 - ✓ Ensure that appropriate IT safeguards are in place such that business-related communications can be produced for an audit or investigation if necessary.

What's Next?

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Jeff is the co-leader of our securities enforcement practice. The former regional director of the Philadelphia Regional Office of the US Securities and Exchange Commission (SEC), Jeff defends public companies, financial services firms, and their executives in SEC, self-regulatory organization (SRO), and state enforcement matters.

[Read Jeff's extended profile.](#)

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Kelly is the co-leader of the firm's securities enforcement practice. She previously held numerous national and regional leadership roles at the US Securities and Exchange Commission (SEC), including serving as the acting deputy director of the Division of Enforcement, as leader of the Enforcement Division's nationwide Climate and Environmental, Social, and Governance (ESG) Task Force, and as director of the SEC's Philadelphia Regional Office. Kelly advises and defends public companies, financial services clients, and their executives in SEC, self-regulatory organization (SRO), and state enforcement matters, and in internal investigations. She is admitted in Pennsylvania and New Jersey only, and her practice is supervised by NY Bar members.

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Christine advises investment managers and broker-dealers on financial regulatory matters. She concentrates her practice on securities regulation for a broad range of financial firms including retail asset managers, private fund managers, family offices, broker-dealers, other professional traders, and high-net-worth individuals. Christine also counsels legal, compliance, and business personnel on the structure, operation, and distribution of advisory programs, including digital advisory offerings, and investment products, including hedge funds, private equity funds, venture capital funds, real estate funds, and other alternative investment products.

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Jedd focuses on global private investment funds and managed accounts, particularly global hedge, private equity, secondary, and venture capital funds. As co-leader of the global private funds practice, he represents leading financial institutions, fund managers, and institutional investors in their roles as fund sponsors, placement agents, and investment entities. He assists clients through all stages of product development and capital raising as well as customized arrangements, seed and lead investor arrangements, and joint ventures. He specializes in all aspects of secondary transactions, and complex financial structurings.

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Gina defends companies involved in a broad array of complex and high-stakes employment disputes. Gina regularly handles discrimination, harassment, retaliation, wrongful termination, whistleblower, and compensation claims as well as ERISA class actions and benefits-related matters. Her ERISA practices includes individual claims and complex class action matters involving defined contribution and defined benefit plans, retirement investment options, insurance products, and severance plans. In addition to litigation, Gina also represents employers and fiduciaries in investigations brought by the DOL.

[Read Gina's extended profile.](#)