

## A Publication of Seward & Kissel Regulatory Compliance

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### Private Equity Adviser Settles Charges of Improper Expense Allocations

The SEC recently agreed to [settle](#) with a registered investment adviser and its principal in connection with improper expense allocations and failure to disclose certain conflicts of interest and related party transactions with the adviser's affiliates and private funds. The adviser improperly charged its private equity fund clients for certain portfolio company expenses and failed to properly offset its management fees with service fees it received from portfolio companies as required by the limited partnership agreement. In addition, the adviser improperly used the funds' assets to pay for the adviser's expenses, including employee salaries, rent and the cost of the adviser's regulatory obligations.

### SEC Chairman Issues Statements on Cybersecurity

SEC Chairman Jay Clayton recently [issued](#) a statement discussing the importance of cybersecurity to the agency and market participants and detailing the agency's approach to cybersecurity. Notably, the statement described a 2016 cyber intrusion of the agency's EDGAR test filing system that may have provided the basis for illicit gain through trading. According to the statement, the intrusion did not result in unauthorized access to personally identifiable information, jeopardize the agency's operations, or result in systemic risk. In a subsequent [update](#), however, Chairman Clayton disclosed that an EDGAR test filing accessed by third parties as a result of the intrusion contained the names, dates of birth and social security numbers of two individuals. The SEC emphasized its commitment to regularly review whether its data protections are appropriate in light of the sensitivity of the data it collects and the associated risks of unauthorized access.

### SEC Releases Risk Alert on the Most Frequent Advertising Rule Compliance Issues

The SEC's Office of Compliance Inspection and Examinations recently released a [Risk Alert](#) on the most frequently identified compliance issues relating to the Advertising Rule under the Investment Advisers Act of 1940. These issues included misleading performance results, misleading one-on-one presentations, misleading claims of compliance with voluntary performance standards, cherry-picked profitable stock selections, misleading selection of recommendations, and a lack of compliance policies and procedures designed to prevent deficient advertising practices. The Risk Alert also provided a summary of observations from OCIE's "Touting Initiative," which examined the adequacy of disclosures that advisers provided when

touting awards, promoting ranking lists or identifying professional designations. Seward & Kissel's memorandum on the Risk Alert is available [here](#).

### SEC ALJ Dismisses Fraud Claim

An SEC Administrative Law Judge recently [dismissed](#) fraud claims against an investment adviser and its principal. The SEC had alleged that the respondents fraudulently reported misleading values for fund assets in violation of GAAP and concealed material information, resulting in higher management fees and other payments. The Administrative Law Judge, however, found that the violations alleged by the SEC are unproven, no material information was concealed from the funds' sophisticated investors, and non-compliance with GAAP by itself is insufficient to prove fraud.

### CFTC Settlement for Failure to Supervise Fund Administrator

The CFTC recently [settled](#) an enforcement proceeding against a registered commodity pool operator ("CPO") for failure to diligently supervise its fund administrator's operation of the commodity pool's bank account containing participants' funds. These failures delayed the detection of ongoing fraudulent withdrawals made by an unknown party who spoofed the CPO's managing member's email address and sent requests that imitated, in some respects, the CPO's typical transfer requests. The fraudulent withdrawals resulted in the loss of \$5.9 million, or 64%, of the pool's funds.

### SEC Settles with Outsourced CCO

The SEC recently [settled](#) an enforcement proceeding against an outsourced CCO of two affiliated advisers. The CCO relied on the adviser's estimates of assets under management and client account numbers when filing Form ADV, and by doing so, did not take sufficient steps to ascertain the accuracy of those numbers. Further, the SEC found that the CCO caused the report to falsely represent that the chief investment officer attested to the accuracy of that information.

### Key Upcoming Compliance Dates

- Form 13F (November 14)
- Form BE-185 (November 14)
- TIC Form S (November 15, December 15)
- TIC Form SLT (November 24, December 26)
- Quarterly update to Form PF for all "large hedge fund advisers" (November 29)

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