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## **SEC Staff Member Speaks on the SEC's Approach to Examining Newly-Registered Private Equity Advisers**

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Carlo di Florio, Director of the Office of Compliance Inspections and Examinations ("OCIE") at the SEC, recently addressed the Private Equity International Private Fund Compliance Forum and answered various questions regarding how the SEC will prepare for and examine the nearly 4,000 newly-registered private fund advisers that registered with the SEC as a result of the recent deadline under the Dodd-Frank Act. Some of the highlights of Mr. di Florio's speech follow.

Mr. di Florio described how OCIE's National Examination Program ("NEP") attempts to manage and mitigate risks presented by private equity funds, as well as large hedge funds, through a three-fold examination strategy. First, the NEP will have a phase of industry outreach and education. Next, there will be coordinated examinations of a large percentage of new registrants, focusing on high-risk areas of their business. Finally, the NEP will publish a series of "after-action" reports on themes and issues identified.

Mr. di Florio indicated that one of the focuses of the NEP is to educate investment advisers regarding compliance, including adopting and implementing written policies and procedures, designating a Chief Compliance Officer ("CCO"), maintaining certain books and records, filing annual updates of Form ADV, ensuring that advertising complies with regulatory rules and implementing a code of ethics. He also noted that NEP's purpose includes strengthening OCIE's communications with senior management of private equity firms in order to assess the corporate culture set at the top of the organization's, senior management's and firm principal's support for CCOs, firms' approaches to enterprise-wide risk management and identification of industry-wide risks.

To identify which candidates to select for examination, the NEP will seek to identify firms and practices that present the greatest risk. Mr. di Florio gave examples of basic risk characteristics that the NEP would be likely to track, including material changes in business activities, changes in key personnel, the regulatory history of the firm and anomalies in key metrics such as fee or performance information.

Mr. di Florio recommends that, in order to avoid attracting NEP attention and potential examination, firms should be proactive about identifying conflicts and remediating those conflicts with strong policies. Furthermore, he commented that firms should also place importance on creating a firm-wide ethical culture. In the case of an examination, a firm should possess strong records and know how to readily access data, document ongoing monitoring and testing of policies and procedures, and be forthcoming about problems.

If a firm is selected for examination, Mr. di Florio noted that the examination itself will generally focus on three



key inquiries: Is the firm's process for identifying and assessing potential problems and conflicts of interest effective? Is that process likely to identify new problems and conflicts that may occur as the future unfolds? How effective and well-managed are the firm's policies and procedures, as well as its process for creating and adapting those policies and procedures, in addressing potential problems and conflicts?

The full address by Mr. di Florio is available [here](#).