ALERT

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# SEC's Focus on Retail Investors Targets Financial Conflicts of Interest

***Initial results of the SEC's Share Class Disclosure Initiative indicate a heightened focus on disclosures made to retail investors and consequences for any failure to self-report.***

On February 12, 2018, the U.S. Securities and Exchange Commission launched its "Share Class Selection Disclosure Initiative" ("SCSDI"), which provided incentives to investment advisers to self-report violations of the federal securities laws related to undisclosed conflicts of interest in mutual fund share class selections. In establishing the initiative, the SEC warned that any failure by a firm to self-report under the initiative would likely result in even more significant sanctions.

Thirteen months later, on March 11, 2019, the SEC announced the results of the initiative: settled charges filed against 79 investment advisers returning more than $125 million to investors. The SEC's orders generally found that the investment advisers placed clients in mutual fund share classes that charged recurring fees deducted from the funds' assets, even though lower-cost share classes were available. This benefited the investment advisers and their affiliated broker-dealers at the expense of their clients, and the advisers' disclosure of this conflict was inadequate.

## Key Points

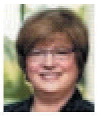
- The SEC staff continues to evaluate self-reports received prior to the initiative cut-off date. The public announcement did not address instances involving allegedly wrongful conduct that were not self-reported. Where it can establish such allegations, the SEC may file additional cases that impose civil penalties to demonstrate consequences for not self-reporting.

- The initial SCSDI announcement indicated that these potential conflict of interest issues had also been identified through the National Exam Program and were featured in a 2016 OCIE Risk Alert. In light of the SCSDI, it is unlikely that firms that have these kinds of conflict of interest issues identified in routine examinations will be permitted to remediate the deficiencies solely through the OCIE program.

- Initiatives such as the SCSDI provide a broad mechanism for the SEC to address what it believes to be wrongful market-related conduct while conserving resources. In an environment in which there are intense budgetary pressures and an immense focus on enforcement numbers—combined with the loss of one month of enforcement activity due to the partial government shutdown—expect the Enforcement Division to continue to identify other potential initiatives that could provide a path to streamlined resolutions.

David P. Bergers
Boston

Sarah L. Levine
Washington



Laura S. Pruitt
Washington

Shamoil T. Shipchandler
Dallas / Houston

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