



# Exclusive: SEC subpoenas employees in books-and-records sweep

*'You've got to make sure that employees understand what the rules are,' expert warns*

By **Bill Myers** - February 4 2022

The **SEC** is conducting an examination sweep to determine whether private fund advisers are complying with the Commission's books and records rules, **RCW** has learned.

Exam questions—and, in a few cases, early-stage enforcement actions—focus not just on firm's policies and procedures, but also on how they monitor for compliance with the books and record rules. In some instances, regulators have drawn employee names at random and subpoenaed texts and messages from their personal phones, tablets and computers, sources tell **RCW**.

“This is a big issue,” says **H. Gregory Baker**, a former SEC enforcement lawyer who now chairs **Patterson Belknap's** securities litigation group. “I think it's going to be one of the headline stories of this year,” he adds.

The Commission promised the sweep in December, after it announced a whopping \$125 million settlement with **J.P. Morgan Securities** over firm employees using applications like **WhatsApp**, text and personal email accounts to conduct business (**RCW**, Dec. 23, 2021). On Jan. 27, the SEC released the second-ever **risk alert** for private funds. Among the problems regulators flagged: books and records compliance.

## 'Aggressive' scope



Baker

Even so, some experts say they are surprised by the scope of the SEC's inquiry.

“The SEC has been really aggressive,” says **Jamie Masella**, a partner with Patterson Belknap. At least three different clients are facing early-stage Enforcement Division investigations over books-and-records, he says. A fourth person, an employee at a large investment bank, was selected—seemingly at random—to have his personal device download, Masella says.

The stakes here are high, Masella says.

“There's no *scienter* requirement for a books-and-records violation,” he says. “” and what the consequences can be. They could be career-ending.”

## Ramp up

*Masella*

Among the lessons Baker and Masella draw are that it's time to update your P&Ps. But it's also time to get aggressive about monitoring and enforcing them.

“I’m not sure, given the attention this issue has been given, that you should do just an annual certification,” Baker says. “Sometimes you hear employees say, ‘Well, I didn’t know I couldn’t do this.’ That’s not going to be an acceptable excuse for the SEC. If the SEC finds enough violations, they’re going to hold the investment adviser responsible.”

Baker and Masella suggest you conduct quarterly reviews and trainings to make sure everyone understands what’s at stake here. They also recommend either providing company phones or demanding that your employees give you access to their communications on their personal phones.

## **‘Ruthless’ enforcement**

**Matt Smith** is the CEO of **SteelEye**, a compliance consulting firm based in the UK. He says that J.P. Morgan actually deserves a little credit for getting ahead of the SEC’s investigation. When it learned that top executives were using secret messaging apps, JP Morgan fired them, Smith says.

“If you don’t enforce the policy, you don’t have a policy,” he says. “So check a box for J.P. Morgan.”

The key question to answer when considering any communications policy, Smith says, is whether your firm can monitor the communications.

“If you’re unable to monitor it, banish it,” he says. “And enforce it. You’ve got to be ruthless with it if you want the regulators to see you’re taking it seriously.”

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