New SEC Technology to Focus on Suspicious Corporate Disclosures

by Dan Brecher on February 26, 2013

The Securities and Exchange Commission (SEC) is increasingly turning to technology to help root out fraud. The agency recently announced plans to launch a new computer software program that will detect accounting anomalies in corporate disclosures submitted to the regulator.

The new data driven approach is expected to bolster the SEC's risk assessment process when it comes to accounting fraud. Under the "Accounting Quality Model" (AQM), the SEC will be able to analyze a company's financial disclosures and assign a specific risk score, which will be used to identify outliers. "It is a model that allows us to discern whether a registrant's financial statements stick out from the pack," Craig M. Lewis, Chief Economist and Director, Division of Risk, Strategy, and Financial Innovation, stated in a recent speech.

In many ways, AQM is similar to the agency's "Aberrational Performance Inquiry" initiative, which focuses on hedge fund advisers. Performance that is flagged as inconsistent with a fund's investment strategy or other benchmarks forms a basis for further investigation and scrutiny. The program has resulted in several successful enforcement cases against advisers since it was first launched in 2011.

However, unlike the program targeting advisers, the SEC plans to use AQM across the SEC to assess the degree to which registrants' financial statements appear anomalous. As Lewis notes, the data it churns out can be useful to a number of groups within the SEC. For instance, the Office of Compliance, Inspections, and Examinations could use these analytics during registrant examinations, and the Enforcement Division could use the analytics to focus their investigative process.

As this new program highlights, the SEC is committed to making good use of the wealth of information it collects. Therefore, it is even more important for regulated entities to devote significant time, money, and effort to compliance activities.

If you have any questions about the SEC's new analytical tools or would like to discuss how they may impact your compliance activities, please contact me, Dan Brecher, or the Scarinci Hollenbeck attorney with whom you work.