

Special Alert

September 14, 2023

Investment Advisors: Assessing Risks, Scoping Examinations and Requesting Documents



The SEC Division of Examinations (the “Division”) issued a Risk Alert on September 6, 2023 that describes the Division’s risk-based approach for selecting advisers to examine and outlines the scope of areas to be examined. Investment advisers may be selected for examination in order for the Division to evaluate risks at a particular firm, risks applicable to investors and the markets broadly, as well as to assess how investment advisers are adapting to new regulatory requirements. In identifying risks, the Division utilizes technology to analyze industry-wide and firm-wide data, as well as reviews regulatory filings (e.g. Form ADV, Form PF).

Selecting Firms to Examine

The Division may select an investment adviser for examination due to characteristics specific to the investment adviser, or based on a tip or complaint. In addition, the Division may examine advisers that provide services or otherwise engage in businesses or practices that are delineated as focus areas by the Division in the annually published examination priorities. Firm-specific factors the Division considers when selecting advisers for examination include the following:

- Prior examinations, especially when the Division observes repetitive deficient practices during more than one review of an investment adviser – including:
 - Significant fee and expense related issues; and
 - Significant compliance program concerns;
- Disciplinary history of associated individuals or affiliates, which gives rise to supervisory concerns;
- Business activities that create conflicts of interest, including outside business activities and dually registered investment advisers and/or personnel;
- Length of time since an investment adviser’s last examination, including newly registered investment advisers;
- Material changes to the firm’s leadership/personnel;
- New reports that involve or impact an investment adviser;
- Disclosure history of the investment adviser; and
- Whether the investment adviser has access to client and investor assets and/or presents certain gatekeeper or service provider compliance risks.

Selecting Examination Focus Areas

The scope of an examination and the documents requested will vary depending upon the investment adviser’s business model, risks and the reason for conducting the examination. Examinations typically include reviews of the following:

- Operations;
- Disclosures;
- Conflicts of interest;
- Compliance practices, specifically including –
 - Custody;
 - Valuation;
 - Portfolio management;
 - Fees and expenses; and
 - Brokerage and best execution.

Typical Documents/Information Requested

Generally, the Division sends an investment adviser an initial request list identifying information and documents to be provided to the Division. The initial request list typically includes:

- General information regarding the investment adviser’s business and investment activities –

- Entity and employee organizational charts;
 - Committee structures;
 - Forms of client agreements;
 - Sub-adviser, third-party manager and other vendor relationships and agreements;
 - Any pending, threatened or settled litigations; and
 - Remedial actions against supervised persons.
- Information about the compliance risks that the investment adviser has identified and the investment adviser's written policies and procedures to address these risks –
 - Compliance policies and procedures;
 - Testing
 - Compliance consultant reports;
 - Annual reviews;
 - Branch office supervision/oversight process;
 - Inventory of compliance risks that form the basis of the compliance program;
 - Employee training;
 - Valuation related issues and processes;
 - Cybersecurity and privacy related information and documentation.
 - Information to facilitate testing regarding trading activities –
 - Client advisory account information – type of account, balance, discretionary authority, investment strategy, investment objectives;
 - Securities held in client portfolios;
 - Any outside compensation relating to clients' transactions and investments;
 - Trade blotter;
 - Wrap fee programs;
 - Trade errors;
 - Trade allocation; and
 - Code of Ethics reporting and reviews.
 - Information to assist the Division in completing testing for compliance in various areas –
 - Advertising;
 - Client meeting materials;
 - Client performance information;
 - Composite performance information;
 - Testimonials and endorsements, including paid compensation;
 - Third-party ratings and rankings; and
 - Financial records of the investment adviser.

Here is the link to the Risk Alert: <https://www.sec.gov/files/risk-alert-ia-risk-and-requesting-documents-090623.pdf>

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compliance programs customized to your particular business demands and operational realities. We offer these services, all as an affilte of a coast-to-coast, full-service law fim.

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