

SEC Risk Alert: Investment Adviser Examinations

SEPTEMBER 14, 2023

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On September 6, 2023, the U.S. Securities and Exchange Commission (SEC) Division of Examinations (the Division) released a risk alert (the Alert) intended to provide SEC-registered investment advisers (advisers) with a new level of insight and additional transparency regarding the scope of adviser examinations, including how the Division assesses risk and selects which firms to examine, and the methodology for document requests during an examination.^[1]

SELECTING FIRMS TO EXAMINE

The Division utilizes a dynamic risk-based approach for selecting advisers to examine and in determining the scope of risk areas to examine, which adapts to changes in market conditions, industry practices, and investor preferences. Each year, the Division publishes its annual priorities,^[2] providing advisers with insight regarding those areas that the Division believes present potential risks to investors and the integrity of the U.S. capital markets. When selecting advisers to examine, the Division considers factors such as which advisers provide services, recommend products, or otherwise meet criteria relevant to the focus areas described in the Division's priorities.

There are also firm-specific risk factors that the staff considers when selecting advisers for examination, such as those related to a particular adviser's business activities, conflicts of interest, and regulatory history. In the Alert, the Division lists 11 firm-specific factors it may consider:

1. Prior examination observations and regulatory history;
2. Supervisory concerns, such as disciplinary history of associated individuals or affiliates;
3. Tips, complaints, or referrals involving the firm;
4. Business activities of the firm or its personnel that may create conflicts of interest;
5. The length of time since the firm's registration or last examination;
6. Material changes in the firm's leadership or personnel;

7. Indications that the adviser might be vulnerable to financial or market stress;
8. Reporting by news media that may involve or impact the firm;
9. Data provided by certain third-party data services;
10. The disclosure history of the firm; and
11. Whether the firm has access to client and investor assets and/or presents certain gatekeeper or service provider compliance risks.

SELECTING EXAMINATION FOCUS AREAS

Once the Division selects an adviser for examination, the Division conducts additional risk assessment to determine the scope of the examinations, including the particular areas of the business that the examiners will focus their review on. Given the size and variety of the adviser population, the Division tailors the scope of an examination and the documents requested to the firm's business model, associated risks, and the reason for conducting the examination. However, examinations typically include reviewing advisers' operations, disclosures, conflicts of interests, and compliance practices with respect to core areas, including, without limitation, custody and safekeeping of client assets, valuation, portfolio management, fees and expenses, and brokerage and best execution. During an examination, the Division requests documents and information applicable to these core areas to test the effectiveness of advisers' compliance policies and procedures for monitoring, mitigating, and managing such risk.

SELECTING DOCUMENTS TO REQUEST

The Division typically sends an adviser a letter notifying the firm of the upcoming examination, which contains an initial request list identifying certain documents that the Division will review as part of the examination. The Division's initial request for information usually includes the following:

1. General information on the adviser's business and investment activities;
2. Information about the compliance risks that the adviser has identified, and the written policies and procedures implemented by the firm to address such risks;
3. Information to facilitate testing with respect to advisory trading activities; and
4. Information for the staff to perform its own testing for compliance in various areas.

The Division attached a four-page list providing "Typical Initial Information Examiners Request of Investment Advisers" as an additional resource for advisers. See the Alert for the full list.

[1] The subject Alert is available at <https://www.sec.gov/files/risk-alert-ia-risk-and-requesting-documents-090623.pdf>.

[2] Winston & Strawn LLP's client alerts regarding the Division's list of priorities released in 2022 and 2023 are available [here](#) and [here](#), respectively.

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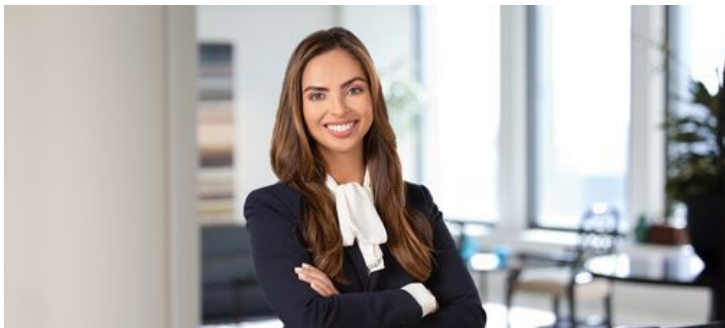
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