**SEC Increases Oversight of Registered Investment Advisers**

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* Recent statements and actions by the Securities and Exchange Commission (SEC) signal the agency will continue to focus its resources and priorities on registered investment advisers, including newly-registered investment advisers (NRIAs).
* A March 2023 Risk Alert focusing on NRIAs, indicates that the SEC is identifying compliance deficiencies in several areas, including policies and procedures, disclosure documents and filings, and marketing.
* Firms engaged in this space will need to look at recent SEC Division of Examinations (the Division) Risk Alerts and revisit past letters to NRIAs in order to position themselves ahead of an SEC examination and proactively assess their compliance program to ensure they continue to meet regulatory requirements and expectations.

**Increasing Focus on NRIAs, Consistent Priorities**

Since taking charge of the SEC in 2021, Chairman Gary Gensler has taken many steps signaling that oversight of investment advisers will continue to be a priority. The SEC’s fiscal year 2024 budget request emphasized the need for additional resources in the Division to address the significant growth in the number of investment advisers and to allow the SEC to adequately examine them within a reasonable time after registration.

On March 27, 2023, the SEC issued a Risk Alert emphasizing that NRIAs are an exam priority. Gensler’s rulemaking agenda has several proposals that would impact investment advisers, including rules regarding the safeguarding of client assets, outsourcing of internal functions, and environmental, social, and governance related disclosures.

Historically, the SEC has provided guidance related to registered investment adviser compliance and issued risk alerts and information to the industry focused on NRIAs. The SEC recognizes that new registrants could benefit from compliance-related guidance in light of the continually evolving financial landscape to ensure that NRIAs have a favorable and well-informed start.

Indeed, nearly a decade ago, the SEC launched an initiative (the “Never-Before Examined Initiative”) to engage with investment advisers that have never before been examined, with an emphasis on advisers that had been registered three years or more. The initiative included risk-assessment and focused review approaches. In the last ten years, the Division has continued to include as a priority topic the examination of NRIAs in its annual Examination Priorities report, including the most recent 2023 Examination Priorities report.[[1]](#footnote-1)

While NRIAs have been a focus of the SEC for the past decade, the recent Risk Alert provides more clarity regarding the expectations and preparation required for their initial examination. This includes highlighting new areas of regulatory scrutiny.

**March 2023 Risk Alert: Focus Areas and Takeaways**

The recent Risk Alert includes a list of the types of information that NRIAs should expect to provide to the Division during an examination and highlights issues that the Division has recently observed from these examinations. Information generally requested during an examination includes:

* General information regarding the NRIA’s business and operations.
* Demographic and other specific data regarding each advisor’s client account.
* Compliance program, risk management practices and framework, and internal controls of the NRIA.
* Communication used by the NRIA to inform or solicit new and existing clients.

Importantly, the Risk Alert indicates that recent examinations have resulted in the SEC concluding that a number of NRIAs are facing compliance deficiencies in the following areas: (1) compliance policies and procedures, (2) disclosure documents and filings, and (3) marketing. While these focus areas continue to touch upon the core and perennial aspects of the SEC’s regulatory regime similar to those identified as part of the Never-Before Examined Initiative, firms should pay particular attention to having appropriate policies, procedures, and controls related to the below topics contained in the Risk Alert in light of recent regulatory attention:

* Use of social media, including approved communication channels.
* Outsourcing certain business and compliance functions.
* Business continuity plans, including succession plans.

Patomak reminds firms that significant attention has been given to the use of social media as evidenced by the recent billion-dollar regulatory fines related to recordkeeping and surveillance violations for employee use of unapproved communication channels. In this regard, it is imperative that firms create a list of approved social media platforms and communication channels and implement controls to ensure employees only communicate on those channels. Firms must also periodically review the list(s) to ensure they continue to be accurate. Firms must ensure that they meet recordkeeping and surveillance requirements related to social media and communication channels as technology continues to evolve.

Additionally, Patomak reminds firms of the recent focus on outsourcing functions to third-parties. In particular, the 2023 Examination Priorities report includes the selection of third-party service providers as a focus area of SEC examinations. In October 2022, the SEC also proposed Rule 206(4)-11 to holistically address oversight of and outsourcing of internal functions to third-parties.

Lastly, due to the increasing changes in the marketplace and the impact of the Covid pandemic, it is imperative that new and existing investment advisers maintain an evergreen business continuity plan. The plans should be tested periodically and updated, as necessary.

**How NRIA’s Can Prepare for Scrutiny**

An NRIA’s first SEC examination provides a valuable opportunity for NRIAs to demonstrate their commitment to compliance with the SEC’s rules and expectations in the short term. It may also impact an NRIA’s ongoing relationship with the SEC, including the scope and timing of future examinations.

To ensure a successful examination, firms should consider the following:

* In responding to an information request, clearly identify the documents provided in response to each request item. The SEC should not have to guess which document is responsive to a request.
* Seek clarification from the SEC if you are not sure what they are asking or if your program does not neatly fit into the way they are asking a question.
* Explain any gaps in information immediately. Do not wait for the SEC to ask.
* Be organized and offer to explain your protocols or clarify a misunderstanding.

Firms should also utilize this opportunity to position themselves ahead of an SEC examination. In particular, an NRIA should proactively assess its compliance program and promptly implement enhancements, as needed, to ensure they are prepared.

Links

* Division of Examinations Risk Alert [https://www.sec.gov/files/risk-alert-newly-registered-ias-032723.pdf] : Observations from Examinations of Newly-Registered Advisers (March 27, 2023)
* Letter to Never Before Examined Investment Advisers [https://www.sec.gov/about/offices/ocie/nbe-final-letter-022014.pdf] (Feb. 20, 2014)
* Information for Newly-Registered Investment Advisers [https://www.sec.gov/divisions/investment/advoverview.htm] (Nov. 23, 2010)
* SEC 2023 Examination Priorities Report

[https://www.sec.gov/files/2023-exam-priorities.pdf] (Feb. 7, 2023)

1. *See, e.g.*, SEC Div. of Examination, Examination Priorities, 5 (Feb. 21, 2013); and SEC Div. of Examination, Examination Priorities, 16 (Feb. 7, 2023). [↑](#footnote-ref-1)