
Ms. Vanessa A. Countryman
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

December 7, 2023

**Re: Request for comment on Safeguarding Advisory Client Assets (Release No. IA-6240; File No. S7-04-23)**

Dear Ms. Countryman:

The Investment Companies Expert Panel[1] on behalf of the American Institute of CPAs is pleased to provide comments to the Securities and Exchange Commission (SEC or Commission) on its proposal on safeguarding advisory client assets, which supplements the AICPA's comment letter dated 8 May 2023.[2]

Our comments address the Commission's proposed Rule 223-1 under the Investment Advisers Act of 1940 (Advisers Act) that would expand the scope of Rule 206(4)-2 under the Advisers Act beyond client funds and securities to include any client assets that are in a registered investment adviser's (RIA's) possession or that the RIA has discretionary authority to trade. The proposal would also add asset verification procedures[3] that would be performed by independent public accountants and would modify the requirements for surprise examinations and notifications to the Commission by independent public accountants.

**Proposed asset verification procedures for client assets unable to be maintained with a qualified custodian**

We understand that the SEC's policy goal in the proposed rule is to prevent misappropriation when client assets are unable to be maintained with a qualified custodian; however, in response to request for comment (RFC) #162, we believe that annual financial statement audits or surprise examinations when audits are not performed, coupled with certain additional investor protections proposed by the SEC in this proposed rule relating to financial statement audits (e.g., prompt reporting of any auditor resignations or other terminations and upon the auditor issuing a modified opinion), are appropriate measures to reduce

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1 The Investment Companies Expert Panel serves the needs of AICPA members on financial and business reporting and audit and attest matters. The Expert Panel protects the public interest by bringing together knowledgeable parties from the investment company industry to deliberate and come to agreement on key issues in the industry.

2 See https://www.sec.gov/comments/s7-04-23/s70423-189381-371982.pdf.

3 The proposed asset verification procedures would require: (1) an RIA to notify the independent public accountant with which it has a written agreement of any purchase, sale, or other transfer of beneficial ownership of privately offered securities or physical assets unable to be maintained with a qualified custodian within one business day, and the independent public accountant would be responsible for performing verification procedures on such transactions promptly and reporting any material discrepancy to the Commission within one business day and (2) all client assets unable to be maintained with a qualified custodian to be verified during the surprise examination or annual financial statement audit rather than permitting such procedures to be performed on a sample basis.

the risk of misappropriation and to deter fraudulent conduct if an RIA is unable to maintain certain client assets with a qualified custodian.[4]

In response to RFCs #159 and #170, performing prompt asset verification procedures on all transactions for client assets unable to be maintained with a qualified custodian, in addition to performing 100% verification procedures of these assets during the surprise examination or financial statement audit, would be costly and challenging to implement without a commensurate benefit. These procedures would require significant additional time to perform risk assessment procedures, which would include obtaining an understanding of internal control,[5, 6] to test potentially immaterial transactions and asset balances, to coordinate with third parties in various geographies and multiple time zones, and to obtain signed, executed agreements, or other documentation regarding proof of ownership for certain asset classes. This additional time would be incurred by staff members to complete and document the work, and multiple senior audit team members would need to be involved to provide appropriate supervision and review over the engagement.[7, 8]

Further, the prompt verification requirement would require auditing firms to implement a "just-in-time" staffing model for these types of engagements, which would be inconsistent with current staffing models used for other engagements and would not be practical. Also, the higher demand on resources would be challenging during "busy season" when resources are in high demand to complete private fund audits for RIAs to meet the SEC's and other regulatory financial statement deadlines and would likely result in resources being reallocated from financial statement audits to complete the prompt verification. As observed in the proposal's Economic Analysis, we agree the higher demand for independent public accountant resources created as a result of the proposed asset verification procedures, including increased time spent by senior audit team members, would increase the cost of independent public accountant services overall. In response to RFC #159, we believe RIAs would pass such costs along to advisory clients. Further, the timing and extent of the proposed asset verification procedures would not be commensurate with the level of risk of material misstatement or misappropriation of client assets unable to be maintained with a qualified custodian, given these assets often consist of privately offered securities (POS) which are typically evidenced by privately negotiated contractual agreements and are not transferable without approval.[9] Also, a practical limitation on the utility of the prompt verification requirement is that if an RIA was engaging in the misappropriation of client assets, the RIA may be less likely to promptly inform the independent public accountant about a fraudulent transaction. As such, the independent public accountant would be unable to perform the verification timely.

The proposed prompt asset verification procedures would also often result in the independent public accountant testing transactions prior to, or concurrently with, the RIA's accounting personnel who are completing their internal review of the transaction documents and the recorded transactions in the books

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4 See also Final rule: Private Fund Advisers; Documentation of Registered Investment Adviser Compliance Reviews ("Private Fund Advisers adopting release"), in which the SEC made several statements that financial statement audits protect investors against the misappropriation of fund assets and provide deterrence against fraudulent conduct by fund advisers or their related persons. For example, the SEC stated: (1) "In addition to protecting the fund and its investors against the misappropriation of fund assets, we believe an audit by an independent public accountant provides an important check on the adviser's valuation of private fund assets, which often serves as the basis for the calculation of the adviser's fees. It also provides an important check on certain conflicts of interest between the adviser and the private fund investors, such as potentially problematic sales practices or compensation schemes" and (2) "Financial statement audits provide meaningful protections to private fund investors by increasing the likelihood that fraudulent activity or problems with valuation are uncovered, thereby providing deterrence against fraudulent conduct by fund advisers or their related persons."

5 Paragraphs .14-.15 of AT-C section 205.

6 Paragraphs .12-.14 and .26-.37 of AU-C section 315.

7 Paragraph .11 of AU-C section 300.

8 Paragraph .35c of AT-C section 105.

9 See, for example, K&L Gates LLP No-Action Letter, which suggests the lack of a risk of misappropriation for loan interests unable to be maintained with a custodian and states, in part, "You represent that Funds do not receive any securities certificate or other tangible token of ownership that could be custodied with its custodian or, that if endorsed and delivered to a subsequent purchaser or other third party, could be used by that third party to evidence its own right to a Fund's Loan Interest. You further represent that possession of the Loan Documents would be of no value to a purchaser or other purported transferee of a Fund's Loan Interests. The Loan Interests are reflected on the records that are maintained on behalf of the Borrower, typically by the Administrative Agent, for the purpose of identifying the owners of all Loan Interests and the principal amount of the Loan attributable to each."

and records. Also, requiring the independent public accountant to test each transaction once notified by the RIA would result in the independent public accountant only having access to transactions reported to them by RIAs rather than to a fulsome set of financial records. As a result, there may be a risk of overreliance on individual transaction detail or on the RIA notifying the independent public accountant of all transactions. As part of a surprise examination and a financial statement audit, an independent public accountant has access to books and records, tests the completeness and accuracy of transactions, and obtains sufficient appropriate evidence, including evidence obtained on a sample basis to support the existence of assets. Such testing is generally performed after an RIA has time to complete its close process for the month, quarter, or year.

In response to RFCs #160 and #161, we believe the Commission should continue to permit sampling in financial statement audits and surprise examinations rather than require 100% testing. Sampling is consistent with current practice for financial statement audits and with the *Commission Guidance Regarding Independent Public Accountant Engagements Performed Pursuant to Rule 206(4)-2 Under the Investment Advisers Act of 1940* issued in 2009 (2009 Guidance),[10] which allows for the use of sampling in the completion of surprise examination procedures. Permitting sampling would better align with the AICPA's attestation and auditing standards, which are required for surprise examinations of RIAs and financial statement audits of private funds, respectively, and require the independent public accountant to obtain reasonable assurance[11, 12] rather than absolute assurance. Independent public accountants regularly use sampling methods[13] during financial statement audits with sampling generally designed to provide a high level of desired confidence.[14] Such methods form the basis for testing and are designed to be both effective and efficient, thereby enabling the independent public accountant to focus on matters most impactful to the users of the surprise examination attestation report and the financial statements, including the auditor's report thereon. Additionally, independent public accountants consider the results of their tests to determine whether testing of the selected sample provides a reasonable basis for conclusions about the population. If independent public accountants find errors during their testing, they either perform additional procedures (e.g., expand their sample to obtain additional evidence, reduce their testing threshold which results in them testing more transactions) or extrapolate the sampling error to the rest of the population to enable them to conclude whether the financial statements, or the subject matter of the examination engagement, are materially misstated.

In a financial statement audit, the auditor designs and performs audit procedures whose nature, timing, and extent are based on, and are responsive to, the assessed risk of material misstatement. Audit procedures typically span throughout the year from planning to year-end, including subsequent events procedures to identify events occurring between the date of the financial statements and the date of the auditor's report that could materially impact the financial statements. In addition to testing the existence of assets, an independent public accountant performs other procedures during an audit (e.g., cash reconciliation testing, other balance sheet testing, income statement testing) and tests transactions during the surprise examination as part of books and records testing to assess compliance with Rule 204-2(b) under the Advisers Act. Such tests are designed to reduce the risk that the auditor will not detect a material misstatement in the financial statements or in consideration of compliance with Rule 204-2(b)

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[10] See Commission Guidance Regarding Independent Public Accountant Engagements Performed Pursuant to Rule 206(4)-2 Under the Investment Advisers Act of 1940.

[11] Paragraph .11 of AT-C section 315 states that, in an examination to examine compliance with specified requirements, the practitioner should seek to obtain reasonable assurance that the entity complied with the specified requirements, in all material respects, including designing the examination to detect both intentional and unintentional material noncompliance. Paragraph .12 of AT-C section 105 defines *reasonable assurance* as a high, but not absolute, level of assurance.

[12] Paragraph .06 of AU-C section 200 states, in part, that, as a basis for the auditor's opinion, the auditor is required to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error. Reasonable assurance is a high, but not absolute, level of assurance because there are inherent limitations of an audit that result in most of the audit evidence, on which the auditor draws conclusions and bases the auditor's opinion, being persuasive rather than conclusive.

[13] Paragraph .05 of AU-C section 530 defines audit sampling (sampling) as the selection and evaluation of less than 100% of the population of audit relevance such that the auditor expects the items selected (the sample) to be representative of the population and, thus, likely to provide a reasonable basis for conclusions about the population.

[14] See the AICPA Audit Sampling Guide. This guide provides guidance to help auditors apply audit sampling in accordance with AU-C Section 530, *Audit Sampling*, and indicates that the concepts and procedures described therein may be useful when performing attestation engagements that involve sampling.

and would be sufficient to reduce the risk that a material misappropriation of client assets is not detected during a financial statement audit or a surprise examination.

**Alternatives to proposed asset verification procedures for client assets unable to be maintained with a qualified custodian**

As we stated above, we believe that annual financial statement audits or surprise examinations when audits are not performed, coupled with certain additional investor protections proposed by the SEC in this proposed rule relating to financial statement audits, are appropriate measures to reduce the risk of misappropriation and to deter fraudulent conduct if an RIA is unable to maintain certain client assets with a qualified custodian. However, if the SEC disagrees and believes it is necessary to provide incremental protections to clients with exposure to these assets, below we are including some less costly alternatives that the SEC could consider adopting, in lieu of the proposed asset verification procedures, to enhance investor protections.

*Second periodic examination for client assets that are unable to be maintained with a qualified custodian and that are held in client accounts that are not audited*

In response to RFCs #158 and #160, for any client account that does not undergo a financial statement audit (e.g., a separately managed account), the SEC could consider requiring during each calendar year a second periodic examination of client assets that are unable to be maintained with a qualified custodian. We believe this alternative could address any concerns that under the current rule, more than 23 months could pass between surprise examinations.[15] A second periodic examination would shorten the period between surprise examinations and enable the independent public accountant to potentially detect in a more timely manner a material misappropriation of client assets unable to be maintained with a qualified custodian.

If the SEC requires a second periodic examination for unaudited client accounts that hold assets that are unable to be maintained with a qualified custodian, we believe such examination should be required to be conducted at a time chosen by the accountant; however, we believe the timing of the second periodic examination, could, but should not be required to, vary from year to year and could be conducted with prior notice to the registrant (i.e., the second periodic examination does not need to be conducted on a surprise basis).[16] This would provide the accountant with flexibility to conduct the second periodic examination at a convenient time when resources are available (e.g., when resources are performing other engagements for the RIA, such as performing interim testing for audits of funds managed by the RIA, or performing other attestation engagements for the RIA) and would provide additional investor protection at a lower cost to investors as compared to the proposed asset verification procedures. Requiring two periodic examinations by independent public accountants, with at least one examination being a surprise and varying in time from year to year, could accomplish the SEC's goal of reducing the likelihood of unidentified material misappropriation of client assets unable to be maintained with a qualified custodian in a more cost-effective way.

If the SEC requires a second periodic examination for unaudited client accounts that hold assets that are unable to be maintained with a qualified custodian, we believe that the scope of the second periodic examination should include: (1) existence and ownership procedures over such client assets as of the periodic examination date, (2) transaction testing of purchases and sales of such client assets and any other transactions that impact client asset balances (e.g., payment-in-kind interest, stock dividends, stock splits, reverse stock splits) for the period covered by the periodic examination, and (3) completeness procedures over the population of transactions for the period covered by the periodic examination.[17] The

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[15] For example, an independent public accountant may have selected January 31, 2022 for the date of the surprise examination in one calendar year and may select December 31, 2023 for the date of the surprise examination in the following calendar year.

[16] We note this is conceptually consistent with Rule 17f-2 under the Investment Company Act of 1940 which permits the independent public accountant to perform one examination with prior notice to the registered investment company.

[17] For example, completeness procedures may include obtaining a listing of transactions and performing a roll forward of transactions during the period covered by the periodic examination.

required existence and ownership procedures should be limited to confirmations with counterparties or counts of physical assets and obtaining documentation regarding proof of ownership to test client assets unable to be maintained with a qualified custodian and should not require confirmation with clients.[18, 19] We believe such testing, in conjunction with the annual surprise examination covering all client assets, would accomplish the SEC's goal of reducing the likelihood of unidentified material misappropriation of client assets unable to be maintained with a qualified custodian.

We recommend the period covered by the second periodic examination should be either the period between the most recent surprise examination and the current second periodic examination or the period between the most recent second periodic examination and the current second periodic examination, whichever is shorter. If the Commission decides to require a second periodic examination, we believe the period covered by the surprise examination should cover the period since the last surprise examination, given the second periodic examination would only cover client assets unable to be maintained with a qualified custodian.[20]

For the second periodic examination that would cover only client assets unable to be maintained with a qualified custodian, we believe that, for the same reasons we described above, sampling should be permitted both in the selection of client accounts that would be subject to testing procedures and in the completion of existence and ownership procedures and transaction testing procedures.

We believe it would be unnecessary to extend the second periodic examination to also cover client assets that are maintained with a qualified custodian given the custodial protections in place when qualified custodians are involved and the costs of these additional procedures that would likely be passed on to investors, which would not be commensurate with the risk.

We also believe audited entities should not be required to have a periodic examination, as we believe a financial statement audit is sufficient to prevent, detect and deter misappropriation of client assets that are unable to be maintained with a qualified custodian and because the costs of a periodic examination, which would likely be passed on to investors, would not justify the benefits. As audits are conducted annually and audited financial statements are required to be provided to investors by the financial statement deadline prescribed by the SEC, the risk that a significant amount of time could pass between audits, like we described above for surprise examinations under current Rule 206(4)-2, is reduced. In addition, as we described above, independent public accountants conducting a financial statement audit

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[18] We do not believe the procedures performed during the second periodic examination should include client confirmations, because a client confirmation typically would not bifurcate client assets maintained with a qualified custodian and client assets unable to be maintained with a qualified custodian. If the second periodic examination involved client confirmation, there would need to be procedures developed to test and reconcile the client confirmation to records distinguishing between client assets maintained with a qualified custodian and client assets unable to be maintained with a qualified custodian, which would be more costly. Furthermore, client confirmation procedures could be more burdensome to clients who are already being asked to respond to confirmation requests during the annual surprise examination of all client assets.

[19] If the second periodic examination is performed "as of" the examination date with procedures limited to confirmations with the counterparties or counts of physical assets, this may have implications on the form of the attestation report. Depending on the text of the final rule, an independent public accountant may not be able to perform a compliance attestation engagement, because the rule may not be prescriptive about requirements for client assets unable to be maintained with a qualified custodian. In such case, the independent public accountant may need to perform an examination engagement in which management makes an assertion related to the existence of client assets unable to be maintained with a qualified custodian and the independent public accountant would examine management's assertion by confirming with counterparties or counting physical assets on a test basis. If the SEC believes timely notification to the SEC by the independent public accountant of a material misappropriation of client assets that are unable to be maintained by a qualified custodian identified during the examination engagement is necessary to reasonably protect investors, we recommend that the Commission require that the independent public accountant notify the Commission within one business day of concluding that such client assets were materially misappropriated.

[20] For example, in 2024, if the surprise examination and the second periodic examination are as of May 31, 2024 and September 30, 2024, respectively and if in 2025, the second periodic examination and surprise examination are as of January 31, 2025 and April 30, 2025, respectively, (1) the period covered by the second periodic examination in 2025 would be October 1, 2024 through January 31, 2025 and (2) the period covered by the surprise examination in 2025 would be June 1, 2024 through April 30, 2025. Alternatively, if, for example, in 2025, the surprise examination and the second periodic examination are as of February 28, 2025 and April 30, 2025, respectively, (1) the period covered by the surprise examination would be June 1, 2024 through February 28, 2025 and (2) the period covered by the second periodic examination would be March 1, 2025 through April 30, 2025.

typically perform testing procedures throughout the year, which may result in the independent public accountant being more likely to detect a material misappropriation of client assets in a more timely manner compared to a surprise examination.

*Quarterly unaudited disclosures*

As an alternative to the proposed asset verification procedures for client assets unable to be maintained with a qualified custodian and in response to RFC #166, the Commission could consider requiring RIAs to provide unaudited quarterly communications to investors in private funds[21] and in other client accounts (e.g., separately managed accounts) that disclose the total dollar value of client assets maintained with a qualified custodian and the total dollar value of client assets unable to be maintained with a qualified custodian. These quarterly investor communications would promote transparency into the proportion of total client assets unable to be maintained with a qualified custodian, which would allow investors in private funds and in other client accounts, who are typically accredited or sophisticated, to raise any questions or concerns about client assets unable to be maintained with a qualified custodian or to perform further diligence with the RIA. We do not believe such quarterly communications should be required to be audited, which would be consistent with recently adopted Rule 211(h)(1)-2 under the Advisers Act which will require quarterly account statements to be sent to investors but will not require such quarterly account statements to be audited.

We believe this alternative would enhance investor protection and is more reasonable from a cost perspective than an alternative requiring an RIA to provide a quarterly summary of a client's transactions involving client assets that are unable to be maintained with a qualified custodian as contemplated by the Commission in RFC #166. We also believe that this alternative is more reasonable from a cost perspective compared to an alternative requiring an RIA to provide quarterly to investors a listing of each client asset held (including whether each client asset is maintained with a qualified custodian or is unable to be maintained with a qualified custodian). If the Commission believes RIAs should provide more detailed information to investors that is incremental to disclosing the total dollar value of client assets maintained with a qualified custodian and the total dollar value of client assets unable to be maintained with a qualified custodian, we believe the Commission should request public comment prior to adopting such a requirement to understand the costs and the implications to investors if RIAs were to disclose their full portfolios.[22]

Additionally, we believe this alternative may be more appropriate and more justified from a cost/benefit perspective for client accounts that do not undergo annual financial statement audits (e.g., separately managed accounts) than for entities that are audited annually.[23] This is because investors in audited entities receive annual audited financial statements that include: (1) an audit opinion about whether the financial statements as a whole are free of material misstatement, whether due to error or fraud and (2) an audited CSOI, at the minimum, which separately lists each investment that exceeds 5% of an entity's net assets (or open derivative contract for which cumulative appreciation or depreciation exceeds 5% of

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[21] For example, such information could be added to the information that would be required to be included in quarterly account statements provided to private fund investors under the recently adopted Rule 211(h)(1)-2 under the Advisers Act or in any other quarterly communication to investors.

[22] For example, FASB Accounting Standards Codification (ASC) 946-210-50-6 requires private funds to disclose in their financial statements a condensed schedule of investments ("CSOI") rather than a full schedule of investments listing each position. A CSOI only requires private funds to disclose individual investments that exceed 5% of a fund's net assets (or open derivative contracts for which cumulative appreciation or depreciation exceeds 5% of a fund's net assets). We note that paragraph B-4 of the basis for conclusions of the AICPA's Statement of Position 95-2, *Financial Reporting by Nonpublic Investment Partnerships* ("SOP 95-2"), which adopted the CSOI requirement despite a full schedule of investments being proposed (and the CSOI being presented in the exposure draft as the minority view), states that "Most respondents to the exposure draft stated that detailed disclosures about the investment portfolio would reveal information, such as trading strategies, that is considered to be confidential." In addition, paragraph B-6 of the basis for conclusions of SOP 95-2 states that "Many respondents stated that investment strategies must be kept confidential to achieve the best result for investors. They expressed concern about disclosing information that they deem to be confidential trade secrets, which might lead other investment firms to "piggyback" the reporting partnership's positions."

[23] We believe this is consistent with the views expressed by the SEC in the Private Fund Advisers adopting release (and also referenced above in footnote 4) that financial statement audits protect investors against the misappropriation of fund assets and provide deterrence against fraudulent conduct by fund advisers or their related persons.

an entity's net assets) and generally categorizes the portfolio by (a) type of investments, (b) country or geographic region and (c) industry.[24] For each audited entity, the auditor is required to perform procedures responsive to the risk of material misstatement of the financial statements of that entity, which includes testing the existence of investments. However, for investors in client accounts whose portfolios are not being audited, quarterly unaudited disclosures of the total dollar value of client assets maintained with a qualified custodian and the total dollar value of client assets unable to be maintained with a qualified custodian would provide additional transparency about the portfolio, and those investors could ask follow-up questions if desired or could divest from the accounts or request the RIA to invest in different asset classes if they have concerns about where the assets are held.

**Commission notification by independent public accountants**

The proposed rule would require the independent public accountant performing an audit to notify the Commission within one business day upon issuance of an audit report that contains a modified opinion and within four business days of resignation or dismissal from, or other termination of, the engagement, or upon removing itself or being removed from consideration for being reappointed. We believe that the RIA, rather than the independent public accountant, should be responsible for notifying the Commission if any of these events occur, since the RIA is principally responsible for compliance with the proposed rule. In addition, the RIA should provide the accountant with a copy of the notification provided to the Commission within one business day. This would be similar to requirements in Rule 17a-5 under the Securities Exchange Act of 1934 for broker-dealers and in Form 8-K for issuers.[25] Consistent with these requirements, we also believe that the independent public accountant should be required to notify the Commission only if the RIA does not self-report or if the independent public accountant disagrees with the content included in the RIA's notification.

**2009 Accounting Guidance**

We recommend the Commission clarify the scope of surprise examination procedures relevant to any adopted rules and more narrowly tailor required surprise examination procedures to the most relevant parts of any adopted rules. The 2009 Accounting Guidance specified that the surprise examination performed by an independent public accountant should cover the RIA's compliance with Rule 206(4)-2(a)(1) and Rule 204-2(b) under the Advisers Act. Rule 206(4)-2 would be redesignated and broadened by proposed Rule 223-1, and Rule 204-2(b) would also be broadened under the proposal. We believe the current surprise examination procedures as outlined in the 2009 Accounting Guidance achieve the Commission's objectives of providing a deterrent against fraudulent conduct by RIAs and are sufficient to detect misappropriation of client assets. As such, we recommend that the Commission clarify that surprise examination procedures should test compliance with proposed Rule 204-2(b)(2)(v) *Transaction and position information* and the portion of proposed Rule 223-1(a)(1)(i) that requires client assets to be maintained with a qualified custodian, because these two portions of the proposed rules most closely align with the current surprise examination requirements. We do not believe that an independent public accountant can or should test the RIA's reasonable belief that various provisions of the written agreement under Rule 223-1(a)(1)(i) have been implemented.[26] Additionally, requiring a surprise examination to

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[24] See FASB ASC 946-210-50-6. In addition, derivatives for which the underlying is not a security are categorized by broad category of the underlying in lieu of being categorized by country or geographic region. Also, while not required by US GAAP, some private funds prepare a full schedule of investments listing each investment in lieu of a CSOI.

[25] For example, under both Rule 17a-5(f)(3) for broker-dealers and Item 4.01 of Form 8-K for issuers, the primary responsibility for direct communications with the Commission upon an auditor termination is on the registered entity (i.e., the registered entity is required to make certain disclosures, and the auditor is required to provide the entity with a letter for it to file with the Commission stating whether the auditor agrees or disagrees with the statements made by the entity). Similarly, under Item 4.02 of Form 8-K, an issuer is required to make certain disclosures if the issuer is advised by, or receives notice from, its auditor that disclosure should be made or action should be taken to prevent future reliance on a previously issued audit report or completed interim review related to previously issued financial statements; the auditor is required to provide the issuer with a letter for it to file with the Commission stating whether the auditor agrees or disagrees with the statements made by the issuer. Likewise, under Rule 17a-5(h), a broker-dealer is required to notify the Commission of certain serious noncompliance with the financial responsibility rules or material weaknesses.

[26] Paragraph .27(b)(ii) of AT-C section 105 requires an independent public accountant, in order to determine that the preconditions for an examination engagement are present, to determine that the criteria are suitable and will be available to the

cover the RIA's compliance with Rule 223-1(a)(1)(i) and Rule 204-2(b) in their entirety would be costly and would go beyond the stated objectives of a surprise examination.

We also recommend that if the Commission adopts a requirement for a second periodic examination for client assets that are unable to be maintained with a qualified custodian and that are held in client accounts that are not audited (as described above), the Commission should provide guidance for such examination (e.g., the type of examination that would satisfy the adopted rule, the scope, the timing, the procedures that should be performed).

Further, to the extent that the 2009 Accounting Guidance is updated to reflect changes from the proposal, we recommend the SEC expose the updated guidance for public comment (e.g., propose guidance with a 60-day comment period concurrently with the adopting release) and adopt final guidance before the compliance date. We believe that because of the importance of the guidance, due process would be valuable. In addition, we believe public feedback would be needed since the proposed rule would apply to all client assets, not just to client funds and securities. Furthermore, it is difficult for the public to provide recommendations in comment letters without clarification of the scope of the surprise examination related to compliance with Rule 223-1 and Rule 204-2(b) and without knowing whether the Commission will adopt any alternatives suggested by commenters.

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We would be pleased to discuss our comments with the Commission or its staff at its convenience.

Very truly yours,

Jaime Eichen, Chair
Investment Companies Expert Panel

Daniel Noll, Vice President
Financial Reporting, Forensic and Valuation Services

Copy to:

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intended users. Evaluation of an RIA's reasonable belief would likely not meet the measurability characteristic of suitable criteria under paragraph .A44 of AT-C section 105, which states the criteria permits reasonably consistent measurements, qualitative or quantitative, of underlying subject matter.