



NATIONAL EXAM PROGRAM

RISK ALERT

By the Office of Compliance Inspections and Examinations¹

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In this Alert:

Topic: Initiative to Examine Registered Investment Advisers Operating from Multiple Locations

Key Takeaways: Staff intends to focus on registered investment advisers that provide advisory services from multiple locations. The examinations will focus on evaluating the design and effectiveness of advisers' compliance programs with respect to their oversight of advisory services provided at remote locations.

MULTI-BRANCH ADVISER INITIATIVE

I. Introduction

The Office of Compliance Inspections and Examinations' ("OCIE") 2016 Examination Priorities include examining the supervisory practices of SEC-registered investment advisers over advisory personnel in branch offices.² OCIE is issuing this Risk Alert to provide additional information concerning its Multi-Branch Adviser Initiative.

II. Background

OCIE examines SEC-registered investment advisers to, among other things, determine whether they are in compliance with the federal securities laws, particularly the Advisers Act. In recent years, OCIE staff (the "staff") has observed an apparent increase in the use of investment advisers employing a business model with numerous branch offices and operations geographically dispersed from the adviser's principal or main office. The use of a branch office model can pose

unique risks and challenges to advisers, particularly in the design and implementation of a compliance program and the supervision of people and processes in branch offices. Accordingly, OCIE is launching the Multi-Branch Adviser Initiative to examine investment advisers operating out of multiple branch offices to determine whether they are in compliance with the federal securities laws in light of the additional and unique risks that arise as a result of operating in this manner.

¹ The views expressed herein are those of the staff of the Office of Compliance Inspections and Examinations, in coordination with other Securities & Exchange Commission ("SEC or "Commission") staff, including staff of the Division of Investment Management. The Commission has expressed no view on its contents. This document was prepared by the SEC staff and is not legal advice.

² See OCIE, "[Examination Priorities for 2016](#)" (January 11, 2016). For purposes of this initiative, when using the term "branch" office the staff is generally referring to a place of business other than the adviser's principal office and place of business at which the investment adviser regularly provides advisory services, solicits, meets with, or otherwise communicates to clients. Cf. Rule 222-1 under the Investment Advisers Act of 1940 ("Advisers Act").

III. Examinations

Multi-Branch Adviser Initiative examinations will focus on advisers' compliance programs and the oversight of investment advisory services provided at branch offices. Additional focus areas may be chosen for review based on the activities or operations of a particular investment adviser.

- **Compliance Programs.** The Advisers Act "Compliance Rule" requires registered advisers to adopt and implement written policies and procedures reasonably designed to prevent and detect violations of the Advisers Act and rules by the investment adviser and their supervised persons.³ The staff will evaluate the design and effectiveness of an adviser's compliance program with respect to its oversight of advisory services provided at its branch offices. In particular, through interviews and the review of advisory records, the staff will assess, among other things, the:
 - Implementation of policies and procedures in the main and branch offices;
 - Supervision structure, including an assessment of how such supervision is tailored to the unique risks in particular branches;
 - Role and empowerment of compliance personnel charged with overseeing branch offices, including their level of access to documents and relevant information; and
 - Accuracy of information on the adviser's filings regarding branch offices, including Form ADV, as compared to actual practices.

In addition, the staff may focus attention, based on the particular business activities of an examined adviser, on assessing compliance and testing controls in one or more of the following risk areas:

- **Fees and Expenses.** The adviser's calculation of fees and other expenses, including the effectiveness of controls over the billing and invoicing processes and communications with clients.⁴
- **Advertising.** Controls over advertisements, such as the adviser's process for reviewing and approving advertisements, particularly those created or disseminated by its branch offices.⁵
- **Code of Ethics.** The implementation of the adviser's code of ethics, including oversight and monitoring of personal securities transactions and whether advisers have properly identified access persons at branch offices.⁶

³ Rule 206(4)-7 under the Advisers Act.

⁴ Advisers Act §§ 206(4) and 207; *see also* Rule 206(4)-7; *In the Matter of WFG Advisors, L.P.*, Inv. Adv. Act Rel. No. 4441 (June 28, 2016).

⁵ Advisers Act § 206(4); Rule 206(4)-1. In addition, Sections 206(1) and (2) of the Advisers Act make it unlawful for any investment adviser using the mails or interstate commerce, directly or indirectly, "to employ any device, scheme or artifice to defraud any client or prospective client" or to "engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client."

- **Custody**. Compliance with the Custody Rule, including controls related to the identification of accounts over which the adviser maintains custody and the involvement of branch office personnel in making such determinations.⁷
- **Investment Recommendations**. As a fiduciary, an investment adviser has an obligation to act in the best interests of its advisory clients and to identify and disclose any material conflict of interest.⁸ The staff will review the process by which investment advice, including the formulation of investment recommendations and the management of client portfolios, is provided to advisory clients from supervised persons located in branch offices. The staff will focus on policies and procedures and supervisory controls designed to address specific risks presented in a branch office model regarding the provision of advisory services to clients, such as the identification of potential conflicts of interest and the level of autonomy supervised persons have in providing advice.⁹

In addition, the staff may focus attention, based on the particular business activities of an examined adviser, on assessing compliance and testing controls in certain of the following risk areas:

- **Oversight**. Supervision and review of investment recommendations made to clients within specific branch offices and across branch offices, including processes and controls regarding investment authority, suitability of the investment advice, and any due diligence that the adviser has told clients is undertaken with respect to investments.
- **Conflicts of Interest**. Identification, management, and disclosure of conflicts of interest that arise through branch office activities and personnel, including conflicts arising from various compensation arrangements and supervised persons' outside business activities.
- **Allocation of Investment Opportunities**. Allocation of investment opportunities among client accounts, including how branch offices' trading activity is monitored and what disclosures are made to clients regarding trade allocation.

In addition to these primary focus areas, examiners may select additional areas for review based on other risks identified during the course of the examination.

⁶ Rule 204A-1 under the Advisers Act requires investment advisers to have codes of ethics setting forth, among other things, a business standard of conduct. The rule also requires advisers to have provisions in their codes of ethics requiring their supervised persons to comply with applicable Federal securities laws, as defined by the rule.

⁷ SEC-registered investment advisers that have custody of their clients' funds or securities must safeguard those funds as required by the SEC's Investment Adviser Custody Rule (Rule 206(4)-2). The Investment Adviser Custody Rule is designed to provide additional safeguards for investors against the possibility of theft or misappropriation by investment advisers who are registered with the SEC.

⁸ See *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180 (1963).

⁹ See *In the Matter of Michael A. Callaway*, File. No. 3-13356 (Jan. 30, 2009).

IV. Conclusion

In sharing the focus areas for the Multi-Branch Adviser Initiative, OCIE hopes to encourage advisers to reflect upon their own practices, policies, and procedures in these areas and to promote improvements in investment adviser compliance programs.

This Risk Alert is intended to highlight for firms risks and issues that the staff has identified. In addition, this Risk Alert describes risks that firms may consider to (i) assess their supervisory, compliance, and/or other risk management systems related to these risks, and (ii) make any changes, as may be appropriate, to address or strengthen such systems. Other risk besides those described in this Risk Alert may be appropriate to consider, and some may not be applicable to a particular firm's business. The adequacy of supervisory, compliance and other risk management systems can be determined only with reference to the profile of each specific firm and other facts and circumstances.
