



Takeaways from Recent Regulatory Examinations & Enforcement Actions

2023 ANNUAL COMPLIANCE CONFERENCE

WEDNESDAY, AUGUST 23, 2023

Important Disclosures



Please carefully review the following disclosures and limitations of this course.

This course is offered for educational purposes only and should not be considered an engagement with Instructor or Sponsor. This presentation should not be considered a comprehensive review or analysis of the topics discussed today. These educational materials are not a substitute for consulting with an attorney or compliance consultant in a one-on-one context whereby all the facts of your situation can be considered in their entirety.



Although the sponsor of this course, RIA Compliance Consultants, Inc. ("Sponsor"), is an affiliate of a law firm and Sponsor may have an individual on its staff that is also licensed as an attorney providing legal services in a completely separate capacity, Sponsor is **not** a law firm and does **not** provide legal services or legal advice. A consulting relationship with Sponsor does not provide the same protections as an attorney-client relationship.



Key Point: *Taking this educational course does not create an attorney-client relationship or a compliance consulting relationship between you and your Instructor or the program Sponsor. If you have questions about your particular circumstances, we encourage you to discuss them with your compliance professional and/or your attorney.*

Please Read Our Fine Print

- ▶ Instructor and Sponsor make all reasonable efforts to ensure the educational material is current and accurate at the time of presentation. Instructor and Sponsor are not under an obligation to advise you of any regulatory developments or subsequent changes to educational material presented in this IAR CE course.
- ▶ Information provided during this course is provided "as is" without warranty of any kind, either express or implied, including, without limitation, warranties and merchantability, fitness for a particular purpose, or non-infringement. Instructor and Sponsor assume no liability or responsibility for any errors or omissions in the content of the presentation.
- ▶ There is no guarantee or promise that concepts, opinions and/or recommendations discussed will be favorably received by any particular court, arbitration panel or securities regulator or result in a certain outcome.
- ▶ *Key Point: Laws and regulations change over time, and it is impossible to predict how a court, arbitration panel, or securities regulator will act in the future. After taking this course, you should be alert for future regulatory developments.*

Keep in Mind

- ▶ Communication with Instructor is not protected from discovery by third-parties during litigation or regulatory proceedings. Please keep questions during this course in a hypothetical form.
- ▶ Reviewing the slides and/or attending this course does not create a consulting engagement with RIA Compliance Consultants, Inc. A consulting relationship can be established only after the following two events have been completed: (1) our thorough review with you of all the relevant facts pertaining to a potential engagement; and (2) the execution of a written engagement and fee agreement and our advance receipt of any retainer required under such an agreement. The slides and/or course should not be regarded as a complete analysis of the subjects discussed. The information on these slides and in the course should not be relied upon as a substitute for one-on-one compliance advice. Often times, a party needs professional advice that applies to his or her specific situation. Your investment adviser firm should retain a compliance professional and/or attorney to provide you with specific guidance regarding your firm's situation.
- ▶ Key Point: Do not disclose confidential or proprietary information during this course. If you have questions about your particular circumstances, we encourage you to discuss them with your compliance professional and/or your attorney.



NASAA Disclosure

- ▶ NASAA does not endorse any particular provider of investment adviser representative continuing education courses. The content of this course and any views expressed are our own and do not necessarily reflect the views of NASAA or any of its member jurisdictions.

Live Course Requirements

- ▶ Login – If you are attending virtually, you must be logged in during the live presentation under your email address.
- ▶ View Entire Live Presentation – You are required to watch/attend the entire live presentation of the course. If you do not watch/attend the entire live presentation, you will have to watch the recorded version in its entirety.
- ▶ Attendance Codes - As you watch the live presentation, you will receive two attendance codes, each containing three alphanumeric characters. Save these codes. You will need to enter the full six-character attendance code prior to accessing the final quiz.
- ▶ Login – You will need to login into <https://www.CE4Advisers.com> and select this course.
- ▶ IAR Acknowledgement – Sign the IAR CE Acknowledgement & Attestation.
- ▶ Final Quiz - You must complete each lesson and receive a score of 70% on the final quiz (within 3 times) to receive IAR CE credit.



Content Questions & Technical Help

If you have questions about the content of this course or need technical help, please contact us via the email address below:

ContEd@ria-compliance-consultants.com

Your Instructor

Jarrold James, Sr. Vice President

▶ RIA Compliance Consultants, Inc.

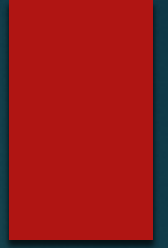
Jarrold has spent his entire career (twenty-two years) working with investment advisers as a compliance professional. His current compliance consulting practice focuses on helping SEC and state-registered firms of all business types and models.

▶ jjames@ria-compliance-consultants.com

▶ 877-345-4034 x 103



Course Overview



- ▶ Regulatory Resources
- ▶ SEC Guidance: 2023 Examination Priorities and Focus Areas
 - ▶ Notable New & Significant Focus Areas
 - ▶ Information Security & Operation Resiliency
 - ▶ Crypto Assets and Emerging Financial Technology
 - ▶ Focus Areas for Examinations of RIAs
- ▶ Pertinent SEC Risk Alerts
 - ▶ New Marketing Rule
 - ▶ Safeguarding Customer Records and Information at Branch Offices
 - ▶ Observations from Examinations of Newly-Registered Advisers
 - ▶ Fee Calculations

Course Overview

▶ SEC Examination Findings – What Are We Seeing?

▶ Different Types of Examinations

- - New Adviser Examination (including RIAs that have not been examined for a number of years – typically focused on a firm's compliance program).
- - Routine Examination
- - Limited Scope/Sweep Examination
- - For Cause Examination

▶ Lots of New Adviser Examinations

▶ Common Deficiencies

▶ Recent Enforcement Action & Takeaways

- ▶ - Monroe Capital Management Advisers > Failing to Disclose Personal Ownership of Investments Recommended to Clients
- ▶ - Jennifer Campbell > Misappropriation of Client Funds
- ▶ - Schwartz > Preferential Treatment for Certain Clients and Cherry-Picking Trades
- ▶ - Sztrom > Unregistered IAR Activity, Violation of Privacy Policy, Misleading Clients

Regulatory Resources

- ▶ *2023 SEC Examination Priorities (2/7/2023):*
 - ▶ <https://www.sec.gov/files/2023-exam-priorities.pdf>
- ▶ *SEC Risk Alert: Examinations Focused on Additional Areas of the Adviser Marketing Rule (6/8/2023):*
 - ▶ <https://www.sec.gov/files/risk-alert-marketing-rule-announcement-phase-3-060823.pdf>
- ▶ *Risk Alert: Safeguarding Customer Records and Information at Branch Offices (4/26/2023):*
 - ▶ <https://www.sec.gov/files/risk-alert-safeguarding-info-branch-offices-042623.pdf>
- ▶ *Risk Alert: Observations from Examinations of Newly-Registered Advisers (3/27/2023):*
 - ▶ <https://www.sec.gov/files/risk-alert-newly-registered-ias-032723.pdf>
- ▶ *Risk Alert: Investment Advisers' Fee Calculations (11/10/2021):*
 - ▶ <https://www.sec.gov/files/exams-risk-alert-fee-calculations.pdf>





Regulatory Resources

- ▶ In the Matter of Monroe Capital Management Advisors, LLC
 - ▶ <https://www.sec.gov/enforce/34-97957-s>
- ▶ In the Matter of Jennifer Campbell
 - ▶ <https://www.sec.gov/files/litigation/admin/2023/ia-6333.pdf>
- ▶ In the Matter of Carl S. Schwartz CPS
 - ▶ <https://www.sec.gov/files/litigation/admin/2023/ia-6320.pdf>
- ▶ In the Matter of Carl S. Schwartz
 - ▶ <https://www.sec.gov/files/litigation/admin/2023/ia-6319.pdf>
- ▶ In the Matter of Michael Sztrom and David Sztrom
 - ▶ <https://www.sec.gov/files/litigation/admin/2023/ia-6296.pdf>

SEC's 2023 Examination Priorities - Notable New & Significant Focus Areas

New Marketing Rule

- ▶ Effective Date = May 4, 2021
- ▶ Compliance Date = November 4, 2022

“The new Marketing Rule is a significant change to a core examination review area for registered investment advisers (RIAs). As such, the Division will, among other things, assess whether RIAs have adopted and implemented written policies and procedures that are reasonably designed to prevent violations by the advisers and their supervised persons of the Marketing Rule. The Division will also review whether RIAs have complied with the substantive requirements of the Marketing Rule, including the requirement that RIAs have a reasonable basis for believing they will be able to substantiate material statements of fact and requirements for performance advertising, testimonials, endorsements and third-party ratings.” (SEC Exam Priorities: <https://www.sec.gov/files/2023-exam-priorities.pdf>)



SEC's 2023 Examination Priorities - Notable New & Significant Focus Areas


RIAs to Private Funds

“.....the Division will continue to focus on RIAs to private funds. In particular, the Division will focus on private fund RIAs: (1) conflicts of interest; (2) calculation and allocation of fees and expenses, including the calculation of post-commitment period management fees and the impact of valuation practices at private equity funds; (3) compliance with the new Marketing Rule, including performance advertising and compensated testimonials and endorsements, such as solicitations; (4) policies and practices regarding the use of alternative data and compliance with Advisers Act Section 204A; and (5) compliance with the Advisers Act Rule 206(4)-2 (Custody Rule), where applicable, including timely delivery of audited financials and selection of permissible auditors.”
(SEC Exam Priorities: <https://www.sec.gov/files/2023-exam-priorities.pdf>)

SEC's 2023 Examination Priorities - Notable New & Significant Focus Areas

Standards of Conduct

- ▶ Regulation Best Interest and Fiduciary Duty
- ▶ Form CRS



SEC's 2023 Examination Priorities - Notable New & Significant Focus Areas

ESG Investing

“RIAs and registered funds are competing for the rising investor demand for ESG-related investments and strategies that incorporate certain ESG criteria, and, thus are increasingly offering and evaluating investments that employ such strategies and investments. Therefore, the Division will continue its focus on ESG-related advisory services and fund offerings, including whether the funds are operating in the manner set forth in their disclosures. In addition, the Division will assess whether ESG products are appropriately labeled and whether recommendations of such products for retail investors are made in investors' best interest.” (SEC Exam Priorities: <https://www.sec.gov/files/2023-exam-priorities.pdf>)

SEC's 2023 Examination Priorities - Information Security and Operational Resiliency

- ▶ Practices to prevent interruptions to mission-critical services and protect investor information, records and assets.
- ▶ Cybersecurity.
- ▶ SEC Proposed Rule: *Cybersecurity Risk Management for Investment Advisers, Registered Investment Companies, and Business Development Companies*
 - ▶ Originally Proposed by the SEC on February 9, 2022
 - ▶ Comment Period Reopened on March 15, 2023
 - ▶ Fact Sheet: <https://www.sec.gov/files/33-11028-fact-sheet.pdf>
 - ▶ Rule Proposal: <https://www.sec.gov/files/rules/proposed/2022/33-11028.pdf>

SEC's 2023 Examination Priorities - Crypto Assets and Emerging Financial Technology

Offer, Sale, or Recommendation of, Advice Regarding and Trading in Crypto and Crypto-Related Assets.

- ▶ Have firms met and followed their respective standards of care when making recommendations, referrals, or providing investment advice, to the extent required?
- ▶ Have firms routinely reviewed, updated, and enhanced their compliance, disclosure, and risk management practices?

Examinations focusing on firms that employ digital engagement practices and the related tools and methods to assess whether:

- (1) Recommendations were made or advice was provided (e.g., through the use of social media marketing and social trading platforms);
- (2) representations are fair and accurate;
- (3) operations and controls in place are consistent with disclosures made to investors;
- (4) any advice or recommendations are in the best interest of the investor taking into account the investor's financial situation and investment objectives; and
- (5) risks associated with such practices are considered, including the impact these practices may have on certain investors, such as seniors.

SEC's 2023 Examination Priorities - Focus Areas for Examinations of RIAs

- ▶ The SEC remains focused on whether the various aspects of RIAs' operations and compliance practices have appropriately adopted and considered current market factors, such as those that might impact valuation and the accuracy of RIA regulatory filings. During a typical examination, the Division reviews the compliance programs and related disclosures of RIAs in one or more core areas, such as:
 1. custody and safekeeping of client assets,
 2. valuation, portfolio management, and
 3. brokerage and execution.
- ▶ SEC Proposed Rule: Safeguarding Advisory Client Assets
- ▶ Originally Proposed by the SEC on February 15, 2023
- ▶ Fact Sheet: <https://www.sec.gov/files/ia-6240-fact-sheet.pdf>
- ▶ Rule Proposal: <https://www.sec.gov/files/rules/proposed/2023/ia-6240.pdf>

- ▶ Often examinations also include a review for conflicts, compliance issues and the oversight and approval process related to RIA fees and expenses, including:
 1. the calculation of fees;
 2. alternative ways that RIAs may try to maximize revenue, including revenue earned on clients' bank deposit sweep programs; and
 3. excessive fees.

SEC's 2023 Examination Priorities - Focus Areas for Examinations of RIAs

- ▶ In addition to reviewing these core focus areas, examinations will review RIA policies and procedures for retaining and monitoring electronic communications and selecting and using third-party service providers.
 - ▶ SEC Proposed Rule: *Outsourcing by Investment Advisors*
 - ▶ Originally Proposed by the SEC on October 26, 2022
 - ▶ Fact Sheet: <https://www.sec.gov/files/ia-6176-fact-sheet.pdf>
 - ▶ Rule Proposal: <https://www.sec.gov/files/rules/proposed/2022/ia-6176.pdf>
- ▶ As in previous years, the Division prioritizes RIAs that have never been examined, including recently registered firms, and those that have not been examined for a number of years. Typically, these examinations focus on firms' compliance programs.



Division of Examinations – Risk Alerts

- Examinations Focused on Additional Areas of the Adviser Marketing Rule (6/8/2023):
- Safeguarding Customer Records and Information at Branch Offices (4/26/2023)
- Observations from Examinations of Newly-Registered Advisers (3/27/2023)
- Investment Advisers' Fee Calculations (11/10/2021)



Different Types of Examinations

- New Adviser Examination (including RIAs that have not been examined for a number of years – typically focused on a firms' compliance programs).
- Routine Examination
- Limited Scope/Sweep Examination
- For Cause Examination

Lots of New Adviser Examinations

- ▶ Typically Performed Remotely
- ▶ Can Occur at Any Time
- ▶ Conducting Brief Introductory Call Before Sending Document and Information Request
- ▶ Approximately 10 – 14 Days to Respond
- ▶ Several Conference Calls and Meetings
- ▶ Exit Interview
- ▶ Deficiency Letter
- ▶ Response Due Within 30 Days

Common Deficiencies

- ▶ Compliance manual not updated for new Marketing Rule Compliance manual not updated for Form CRS/ADV3
- ▶ Form CRS not posted to website
- ▶ Lack of annual compliance review
- ▶ Form ADV Inaccuracies and Insufficiencies
- ▶ Outdated or un-customized compliance manual
- ▶ Undisclosed affiliated service provider
- ▶ Insufficient disclosures and procedures around use of inverse ETFs
- ▶ Not sourcing/crediting the use of third-party created marketing content
- ▶ Insufficient documentation for best execution review
- ▶ Custody – SLOA No-Action Letter Non-Compliance

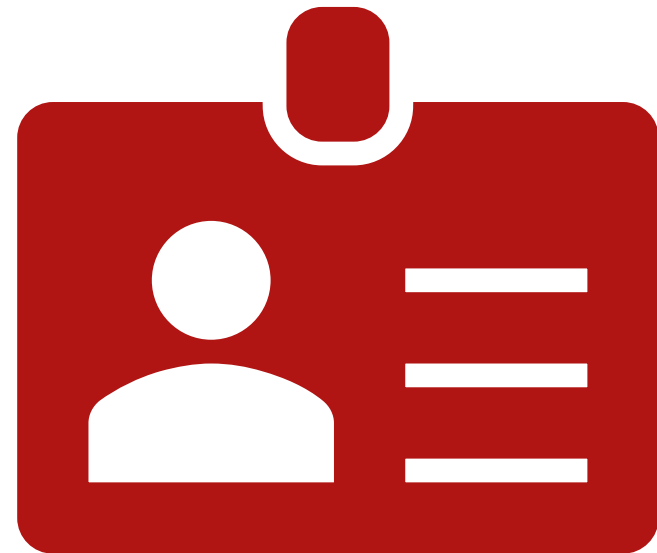
Examinations v. Enforcement

The Division of Examinations conducts the SEC's National Exam Program. The Division's mission is to protect investors, ensure market integrity and support responsible capital formation through risk-focused strategies that: (1) improve compliance; (2) prevent fraud; (3) monitor risk; and (4) inform policy. The results of the Division's examinations are used by the SEC to inform rule-making initiatives, identify and monitor risks, improve industry practices and pursue misconduct.

The SEC's *Enforcement* staff conducts investigations into possible violations of the federal securities laws and prosecutes the SEC's civil suits in the federal courts as well as its administrative proceedings.

Recent Enforcement Actions & Takeaways

- Administrative Proceeding Against Monroe Capital Management Advisers (<https://www.sec.gov/enforce/34-97957-s>)
 - Main Issue: Failing to Disclose Personal Ownership of Investments Recommended to Clients
 - Suggested Takeaway: Conduct a review to determine if all conflicts of interest regarding your Investment Adviser firm's personnel's ownership of investments in which your Investment Adviser firm recommends to clients is supervised and disclosed, as necessary.



Recent Enforcement Actions & Takeaways

- Administrative Proceeding Against Jennifer Campbell (<https://www.sec.gov/litigation/admin/2023/ia-6333.pdf>)
 - Main Issue:
 - Misappropriating funds from clients of the Investment Adviser by making unauthorized changes to client account settings and then forging checks and ACH documentation to misdirect clients fund into her own brokerage accounts.
 - Suggested Takeaways:
 - Involve multiple positions/team members in the process.
 - System of checks and balances, back-end fee audit reviews.
 - Identify tests and audits to be performed ongoing and periodically.
 - Credit checks for key personnel – initially and annually.

Recent Enforcement Actions & Takeaways

- Carl S. Schwartz and Carl S. Schwarz, CPA
(<https://www.sec.gov/litigation/admin/2023/ia-6320.pdf>
and <https://www.sec.gov/litigation/admin/2023/ia-6319.pdf>)
 - Main Issue:
 - Preferential Treatment for Certain Clients and Cherry-Picking Trades
 - Making favorable trades to accounts owned by a new, larger, more lucrative client while disproportionately allocating a number of unfavorable trades to other clients.
 - Suggested Takeaways
 - Personal Securities Transaction reviews.
 - Create automated reports and tests.
 - Different procedures depending on responsibility
 - Pre-approval for certain personnel and situations.
 - Using a team approach to work with clients.



Recent Enforcement Actions & Takeaways

- Michael Sztrom and David Sztrom (<https://www.sec.gov/litigation/admin/2023/ia-6296.pdf> and <https://www.wealthmanagement.com/regulation-compliance/sec-father-and-son-duo-misled-investors>)
 - Main Issue: Unregistered IAR Activity, Violation of Privacy Policy, Misleading Clients
 - Suggested Takeaways: Train supervised persons on privacy and confidentiality, due diligence of new personnel, cross-check for prior registration activity, require reporting of outside business activities of IAR and support staff

Questions

Please submit any question online or email with any questions about the content of this course.

ContEd@ria-compliance-consultants.com

The End.

Thank You