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SEC Publishes the Most Frequent Advisory Fee and Expense Compliance Issues Identified in Examinations of Investment Advisers

On April 12, 2018, the Securities and Exchange Commission's Office of Compliance Inspections and Examinations ("OCIE") published a Risk Alert¹ listing the most frequent advisory fee and expense compliance issues identified in deficiency letters sent to SEC-registered investment advisers ("advisers"). The deficiencies observed by OCIE staff that are most relevant to private fund advisers include:

Expense Misallocations. For example, allocating marketing expenses, regulatory filing fees and travel expenses to private funds instead of to the adviser in contravention of the applicable advisory agreements, limited partnership agreements, private placement memoranda, Form ADV, or other disclosure documents; or allocating broken deal expenses relating to co-investment vehicles to private fund clients in contravention of disclosures.

Use of Incorrect Account Valuations in Fee Billing. For example, valuing client assets using a different metric or process than disclosed, resulting in overbilling of advisory fees.

Disclosure Issues Involving Advisory Fees. For example, collecting expense reimbursements in excess of those disclosed.

Applying Discounts Incorrectly. For example, failing to apply pre-arranged fee discounts to accounts over a certain size.

Billing Fees with Improper Frequency. For example, charging fees on a monthly basis, instead of on a quarterly basis as stated in disclosures; charging fees in advance, despite disclosures specifying that clients would be billed in arrears; or failing to pro rate fees for partial periods.

Key Takeaways. Advisers may want to consider reviewing their advisory fee and expense practices, policies and procedures to ensure compliance with their advisory agreements and disclosures provided to investors. Advisers may also want to consider adopting and implementing written policies and procedures reasonably designed to prevent discrepancies among such practices, advisory agreements and disclosures.²

¹ See National Exam Program Risk Alert "Overview of the Most Frequent Advisory Fee and Expense Compliance Issues Identified in Examinations of Investment Advisers" (April 12, 2018), available at <https://www.sec.gov/ocie/announcement/ocie-risk-alert-advisory-fee-expense-compliance.pdf>.

² See Investment Advisers Act Rule 206(4)-7.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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