

OCIE Observations on Supervision and Compliance for Branch Offices

The Commission's Office of Compliance Inspections and Examinations or OCIE issued a Risk Alert on November 9, 2020 ([here](#)) centered on questions keyed to supervision and compliance in the context of multiple branch advisories. The alert is a combination of observations and deficiencies stemming from nearly 40 examinations of multi-office advisory operations. The Alert provides a good overview of how multi-office advisory operations function and their deficiencies.

Compliance and inspections

The staff observations center on two topics: First, compliance and supervision. Second, investment advice. The "vast majority" of advisers examined were "cited for at least one deficiency related to the Compliance Rule. The observations fall into four groups: 1) inaccurate information tied largely to outdate information from personnel changes and similar changes; 2) an inconsistent application of policies across the firm; 3) inadequate implementation; and 4) no implementation.

Several examples were offered to illustrate the points uncovered.

Custody of client assets. A number of advisers did not have policies and procedures that "limited the ability of supervised persons to process withdrawals and deposits in client" in accounts and make other changes. The staff found that advisers had custody of client assets for a variety of reasons. That in turn resulted in a variety of approaches to dealing with the assets.

Fees and expenses. This is another key area highlighted with examples. In some instances, advisers did not have policies and procedures that covered remediation for overcharges. In other instances, the firm had policies for wrap fees that were not consistently applied. Most of the fee issues observed tied to a lack of oversight.

Supervision. Oversight of supervised persons is another area of concern. The issues tied to failures to disclose material non-public information, portfolio management such as

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recommendations regarding mutual fund shares, and trading and best execution. Another key area involved the oversight of branches that have a higher risk profiles than other offices.

Advertising. A number of issues were presented where the branch operated under a different name from the primary office – a so-called “doing business as” or DBA. Issues arose with respect to performance presentations that omitted material information, unsupported claims, credentials that were not accurate and third-party rankings or awards that neglected to include all material information.

Code of Ethics. Several advisers were cited for deficiencies with respect to their Code of Ethics. The deficiencies generally tied to reporting requirements for transactions and the failure to properly identify access persons. Another group of deficiencies centered on the failure to review and approve procedures before they were put in place.

Advice

The staff observations regarding investment advice center on portfolio management and a series of issues that have largely been covered in other alerts and which, in some instances, have been the subject of enforcement actions. The issues center on question of oversight, conflicts and trade allocations.

Mutual fund share selection was a key issue in this area which frequently tied to oversight and supervision. The issues are exemplified by the share class selection cases – the failure to disclose the fact that certain mutual fund shares pay 12b-1 fees. This is a key disclosure issue that has been litigated repeatedly by Enforcement and was the subject of a significant cooperation program by the Division. This is only one of a number of conflicts observed which, in some instances, have also been the subject of litigation.

Another series of questions were presented by wrap fees. As with the share class selection issue discussed above, this point has been the subject of prior enforcement actions. The points generally hinge on questions regarding the use of the fee with particular clients, compliance with the terms of the arrangement and the failure of the firm to supervise transactions.

A third issue centers on the rebalancing questions. Here questions arose regarding the automated rebalancing of a portfolio after a transaction and whether the arrangement was in fact in the best interest of the client.

A final set of issues focused on trading and the allocation of investment opportunities. In these transactions, advisers were cited for a lack of documentation, completing principal transactions involving securities sold from inventory without client consent and inadequate monitoring.

Conclusion

The Alert concludes with a series of observations by the staff which include: 1) Some

advisers use uniform policies and procedures for monitoring and approving advertising; 2) in a number of instances centralized processes were used for billing, monitoring and approving personal trading, portfolio management, compliance procedures and for training. These observations, coupled with the others in the Alert, serve to give the multi-office advisory a good view of industry practices which can assist in guiding current management and the development of future processes.