

INSIGHTS

## OCIE Releases Risk Alert Regarding the Fees and Expenses that Investment Advisers Charge Clients

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The Office of Compliance Inspections and Examinations (OCIE) of the Securities and Exchange Commission (SEC) recently released a Risk Alert that highlights the most common compliance deficiencies relating to fees and expenses charged by SEC-registered investment advisers.<sup>1</sup> The Risk Alert is drawn from the most frequently observed issues in deficiency letters from over 1,500 adviser examinations completed during the last two years.

OCIE listed the following six deficiencies related to advisory fees and expenses as the most common:

1. *Fee-Billing Based on Incorrect Account Valuations:* OCIE identified overbilled advisory fees as a frequently observed deficiency. For example, OCIE found that advisers valued assets in a client's account using a different metric or process than that which was specified in the client's advisory agreement.
2. *Billing Fees in Advance or with Improper Frequency:* OCIE identified improper billing practices as another area of concern, and in particular, issues with the timing and frequency for which advisory fees were billed, such as billing advisory fees on a monthly instead of quarterly basis as provided in the advisory agreement or disclosed in Form ADV Part 2, and failure to pro rate fees for partial periods.
3. *Applying Incorrect Fee Rate:* Additionally, OCIE observed that some advisers were applying a rate higher than what was agreed upon in their advisory agreements. Moreover, OCIE observed that some advisers charged non-qualified clients performance fees based on a percentage of their capital gains in violation of Section 205(a)(1) of the Advisers Act.
4. *Omitting Rebates and Applying Discounts Incorrectly:* OCIE found that some advisers did not apply certain discounts or rebates to their clients' advisory fees, contrary to the terms of their clients' agreements.
5. *Disclosure Issues Involving Advisory Fees:* OCIE identified several issues related to Form ADV disclosures. For example, OCIE described instances in which advisers made disclosures inconsistent with their actual practices or failed to disclose certain additional fees or markups in addition to advisory fees.
6. *Adviser Expense Misallocations:* OCIE observed improper practices related to the allocation of expenses, such as the allocation of distribution and marketing expenses, regulatory filing fees, and travel expenses to clients instead of the adviser, contrary to applicable

advisory agreements, operating agreements or other disclosures.

Advisers are encouraged to assess their advisory fee and expense practices and related disclosures in order to comply with the Advisers Act and their fiduciary duty to clients. In addition, advisers should review the effectiveness and adequacy of their compliance programs.

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<sup>1</sup> The Risk Alert is available [here](#).