SEC warns advisers to toe the line on fees

A risk alert highlights areas where the commission has seen mistakes and misconduct when it comes to charging fees for financial advice

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By **Jeff Benjamin**

The Securities and Exchange Commission is putting the financial industry on notice that it is looking for advisers who are overcharging their clients.

The risk alert, sent out Thursday morning by the SEC's Office of Compliance Inspections and Examinations, detailed the most frequent **advisory fee** and compliance issues it sees in deficiency letters sent to SEC-registered advisers.

The **four-page alert**, described by some compliance experts as a warning that the SEC is focused on how fees are charged, cited instances of fees being charged on incorrect account valuations and examples of advisers not following the fee guidelines presented in their own Form ADV filings.

The alert also warned advisers about such practices as omitting rebates, applying discounts incorrectly, lax fee disclosures and basic miscalculations of fees.

"I view this as a heads-up to advisers, which the SEC has been doing more frequently," said Amy Lynch, president of FrontLine Compliance.

A former SEC examiner, Ms. Lynch said she has seen various types of billing errors, and said the punishment will usually depend on how long a period the errors went on for and the overall dollar amount of harm to the clients.

"Oftentimes, the billing errors are inadvertent because something might have been set up incorrectly in the portfolio accounting system," she said. "But the key is evaluating it and monitoring it."

The SEC alert cited instances where non-qualified clients — or clients who didn't meet wealth thresholds for certain investments — were incorrectly charged investment-performance fees, and clients in fee-based wrap accounts were charged brokerage fees, among other violations.

Another common violation was advisers not reducing fees when client accounts reached certain breakpoint levels.

Phil Shaffer, founder of Halite Partners, doesn't think the alert goes far enough in terms of keeping advisory firms in line.

"This information should be shared verbally and in sales material, not just hidden in an ADV disclosure that is hard to find and will not be seen by most investors," he said.

Tim Holsworth, president of AHP Financial Services, a dually-registered firm affiliated with Raymond James, said billing problems are most likely the result of a lack of back-office support.

"If you're a true RIA and you do your own billing, and you have less sophisticated systems, that's when these things occur," he said. "I will tell you our billing is down to the penny and we don't have any of those issues. It's the difference between having an international company doing this and a mom-and-pop operation."

That's essentially the way it looks to Todd Cipperman, principal at Cipperman Compliance Services.

"Issues like incorrect valuations, wrong fee rates, and failure to aggregate accounts are oftentimes the result of poor operational and compliance infrastructure rather than intentional misfeasance," he said. "Emerging investment firms are often reluctant to hire back office compliance and operational resources who make sure that these mistakes don't get made."

Barry Temkin, a partner at the law firm of Mound Cotton Wollan & Greengrass, described the alert as a continuation of the amnesty program the SEC introduced under the **Share Class Selection Disclosure Imitative in February**.

While he said the alert offers some "valuable guidance to advisers," Mr. Temkin admitted "some of the issues are just common sense," such as making sure advisory fees comply with the written customer agreement.

"This might be a good opportunity for advisers to take some time to review their fee billings to ensure consistency in their calculation of AUM and attendant fees, which can be tricky," he said. "It's like the dentist reminding patients to brush. This is your warning from the SEC, so take a couple hours, look over the fees, and maybe have someone come in and kick the tires."

That attitude is essentially what the SEC is hoping advisers embrace, according to Peter Driscoll, director of the SEC office that issued the alert.

"Don't overbill your clients," he said. "Basically, bill in accordance with what the agreements say. They lose sight of it, the way markets move, the way markets grow. Firms don't revisit it. That's the big thing."

Kashif Ahmed, president of American Private Wealth, made no excuses for advisers who bungle client fees, and said he encourages clients to review everything and ask questions.

"One would think advisers could get something as simple as this right," he said. "After all, we're in a numbers business. I would hate to think that this is common, but if the SEC is concerned enough to make it an area of focus, that must mean there are enough instances of this activity."