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## How to Become a Registered Investment Advisor

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# Agenda

- Definition of Investment Advisor
- SEC v. State Registration
- Registration Process & Requirements
- Best Practices for Drafting the Form ADV
- Some Common Registration Traps
- Ongoing Compliance Duties of a New Firm

# Definition of Investment Advisor

individual or entity that:

- (1) provides advice or analysis by making direct or indirect recommendations regarding securities or securities markets;
- (2) for compensation in any form; and
- (3) engages in the regular business of providing advice regarding securities.

# Exemption from Registration

- “Solely Incidental” Exclusion for Broker-Dealers, Lawyers, Accountants, Engineers, Teachers, Banks, Bona Fide Publishers
- Private Fund Adviser Exemption
- Some state may have exemption based on limited number of clients

# Who Should Register as IA?

- Recommend Establishing an Entity
- This Entity Will Register as the Investment Advisor
- Individuals Will Register as the Investment Adviser Rep under the Firm



# Investment Adviser Rep

- Definition Differs Depending Whether IAR Rep to State or SEC Firm
- Definition of IA Rep with State Firm Also Varies by State
- Need to Consult Applicable Rules of State Securities Regulator

# General Definition of IAR

A person who, for compensation

- (1) provides any advice or recommendations regarding securities;
- (2) makes investment decisions regarding securities;
- (3) solicits or sells investment advisory services; or
- (4) supervises employees who perform any of the foregoing

## IA Rep Qualifications

- Varies by State
  - Typically Series 65
  - Series 66 & Series 7 Currently Held by B/D
  - In Lieu of Exams: CFP, CFA, ChFC, PFS, CIC currently Active and in Good Standing
- Still Required to File Form U4

# SEC v. State Registration of IA

- Typically Determined by Assets Under Management (AUM)
  - Amount of Assets Receiving Continuous Supervision
  - SEC Registration Allowed at \$100 Million AUM

## SEC Exemptions to \$100M AUM

- 120 Day Exemption
- Investment Company
- 15 States
- Pension Consultant (\$200M)
- Internet Advisor

# SEC Registration Process

- Establish & Fund IARD/CRD Account
- File ADV Part 1A & Applicable Schedules (i.e., Schedules A, B, & D) via IARD System
- Upload ADV Part 2A via IARD System
- Minimal Review by SEC
- Typically Takes Less than 30 Days for SEC to Approve/Deny an Application
- Notice File in Applicable States
- File Form U4s of IA Reps with Applicable States
- Expect SEC Audit within First 6-12 Months of Registration

# State Registration Process

- Establish IARD/CRD Account
- File Application with State Securities Regulator
  - ADV Parts 1A & 1B and Applicable Schedules (i.e., Schedules A, B, & D) via IARD System
  - Upload Form ADV Part 2A & Part 2B via IARD System
  - Financial Statements
  - Sample Client Agreements
  - Misc. State Forms
- File Form U4s of IA Reps
- Intense Review – Will Ask Questions & Require Changes
- Expect Approval /Denial to Take at Least 30 – 45 Days

# States Requiring Registration/Notice Filing

- Generally Required to Register or Notice File in States Where Offices Located or More than Five Clients
- Certain States Do Not Follow This Rule



# States Requiring IAR Licensing

- IARs of SEC Registered Firm
  - File in State Where Offices Located
- IARs of State Registered Firm
  - File in State Where Offices Located
  - File in States Where Firm Exceeds DeMinimis Exemption (At Least 1 IAR Must File in State if Firm Registered in State)
- Certain States Do Not Follow These Rules

# Net Worth Requirements

- SEC Registered Firm
  - Doesn't Require Net Worth or Bond
  - Requires Firm to Maintain Financial Books & Records
  - Must Disclose to Clients Precarious Financial Condition
- State Registered Firm
  - Many States Require a Required Net Worth Depending Upon Whether Firm Has Custody or Discretion
  - This Typically Ranges from \$10,000 to \$35,000 Depending Upon State & Activity
  - Surety Bonds Are Often Allowed as Substitute for Net Worth

## Form ADV - Uniform Form for Investment Adviser Registration

- Form ADV Part 1A
  - Contact Info
  - Basis for Registration
  - Notice Filing States
  - Organization Form
  - Fees & Compensation Arrangements
  - Advisory Activities
  - Advisory Clients
  - Other Business Activities & Affiliated Firms
  - Discretion & Proprietary Transactions
  - Custody
  - Felonies, Investment-Related Misdemeanors, Adverse Regulatory Actions & Court Judgments in Violation of Statute or Regulation

## Form ADV (Cont.)

Schedules A & B – Officers & Ownership

Schedule D – Misc.

Part 1B – State Registered

- States Where Registering
- Supervisory Principal
- Surety Bond
- Unsatisfied Liens, Arbs & Civil Judgments

## Form ADV Part 2

- Advisory services and fees;
- Types of Clients;
- Types of investments;
- Methods of analysis, sources of information and investment strategies;
- Education and business standards required by the firm;
- Education and a minimum of five years of business background for executives of the firm and those that provide investment advice;
- Other business activities;
- Other financial industry activities or affiliations;
- Participation or interest in client transactions;
- Conditions for managing accounts;
- Review of accounts;
- Investment or brokerage discretion; and
- Additional compensation.

# Form ADV Balance Sheet & Appendix 1

- If Balance Sheet Is Required Pursuant to Form ADV Part 2, Item 18
- Form ADV Part 2-Appendix 1-Wrap-fee Brochure-Sponsor Wrap Fee Program
  - Generally, if investment advisory services and custodial/brokerage services are “wrapped” under one fee, the program can be deemed a wrap fee program.

# ADV Drafting Tips

- Know Who Is Completing Form & Who Is a Related Person
- Understand How to Calculate AUM
- Fully Describe Advisory Services & Fees
- Fully Describe OBA of Firm, Reps & Affiliates
- Disclose Potential Conflicts of Interests
- Know What Should Be Disclosed that's Not Included in the Instructions for Part 2

# Common Mistakes

- Failure to Submit Client Agreement or Inconsistent Client Agreement
- Failure to Submit IA Rep Fingerprint Card
- Failure to Submit Adequate Financial Statement or Surety Bond
- Failure to Submit Misc. State Forms
- Failure to Designate CCO
- Failure to License Owner of Firm



## Registration Challenges Facing Lay Person

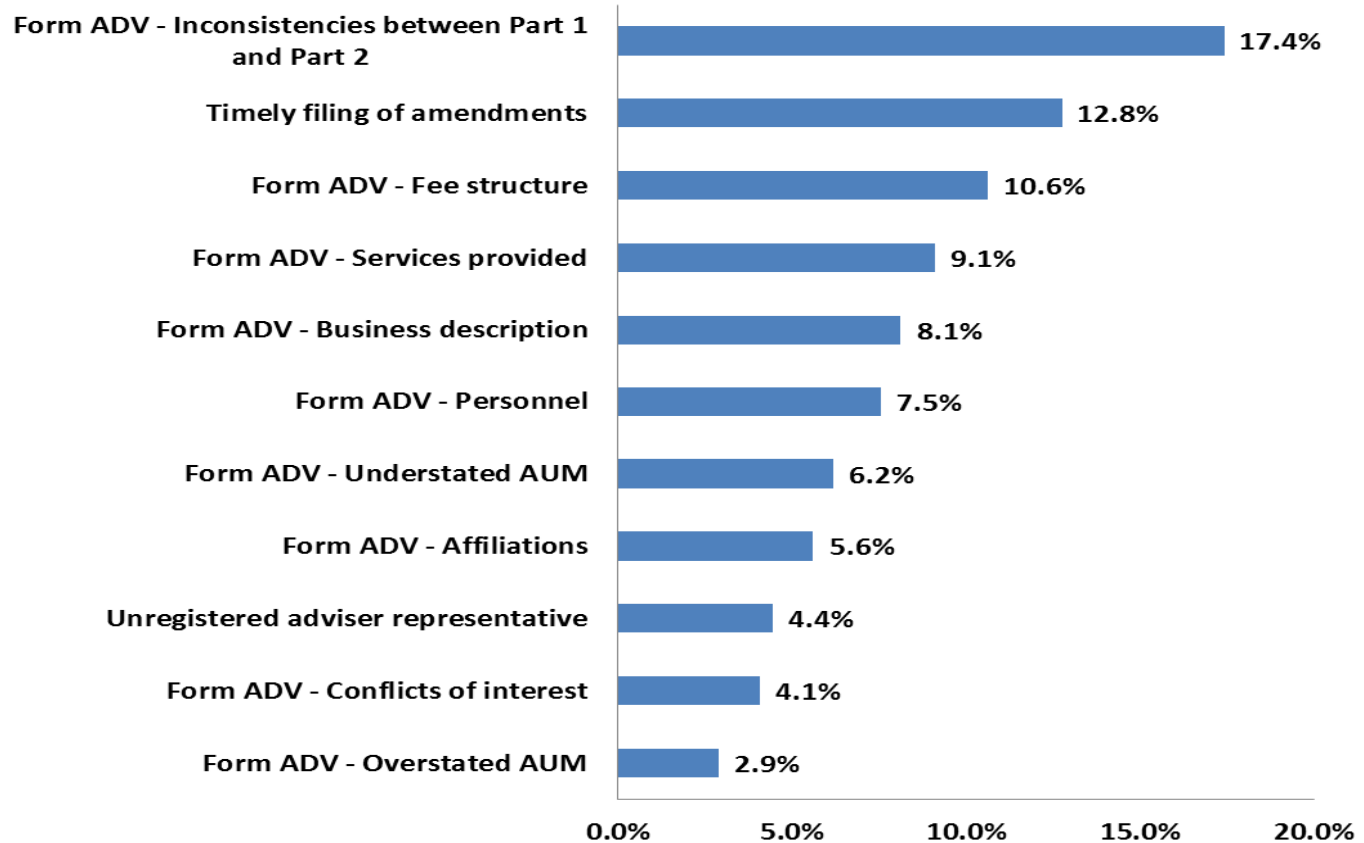
- Knowledge of IA Business Models, Best Practices & Worst Case Scenarios
- Understanding Expectations of a Regulator at Registration & Later During Exam
- Navigating the IARD/CRD System
- Accurately & Thoroughly Answering Form ADV Questions & Miscellaneous Forms
- Consistency Within Form ADV & Between Other Documents
- Disclosing Conflicts & Information Not Specifically Requested but Required
- Communicating with Regulators

# Most Common Exam Violation for Investment Advisors

## NASAA 2015 Investment Adviser Coordinated Exams Report

### Registration

517 Deficiencies  
41.5 % of Advisers with AUM



NORTH AMERICAN SECURITIES ADMINISTRATORS ASSOCIATION

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September 29, 2009

**NASAA Outlines Best Practices For Investment Advisers**  
*Coordinated IA Examinations Spotlight Deficiencies in Key Areas*

WASHINGTON, D.C. (September 29, 2009) – The North American Securities Administrators Association (NASAA) today released an updated series of recommended best practices that investment advisers should consider in order to improve their compliance practices and procedures.

"By identifying these deficiencies, our goal is to help investment advisers minimize the risk for regulatory violations by strengthening their internal compliance programs. Our best practices are designed to assist advisers in meeting compliance challenges while providing better services to their clients," said NASAA President and Texas Securities Commissioner Denise Voigt Crawford.

Crawford said the best practices were developed after a series of coordinated examinations of investment advisers by 35 state and provincial securities examiners revealed a significant number of problem areas. Crawford said examinations of 458 state-level investment advisers conducted between January and May 2009 revealed 1,887 deficiencies in 13 compliance areas.

The 2009 examinations were conducted under the guidance of NASAA's Investment Adviser Operations Project Group. The top five categories with the greatest number of deficiencies involved registration, books and records, unethical business practices, supervision and financials.

The examinations revealed that:

- The top trouble spots in the area of registration were inconsistencies between parts I and II of form ADV and failing to amend form ADV in a timely manner.
- In the area of preparing and maintaining current and accurate books and records, the top deficiencies included not maintaining suitability information, not properly safeguarding records and not backing up data.

“The top trouble spots in the area of registration were inconsistencies between parts 1 and II of Form ADV....”



### Information for Newly-Registered Investment Advisers

Prepared by the Staff of the Securities and Exchange Commission's Division of Investment Management and Office of Compliance Inspections and Examinations<sup>1</sup>

This information sheet contains general information about certain provisions of the Investment Advisers Act of 1940 (also called the "Advisers Act") and selected rules under the Advisers Act. It is intended to assist newly-registered investment advisers in understanding their compliance obligations with respect to these provisions. This information sheet also provides information about the resources available to investment advisers from the SEC to help advisers understand and comply with these laws and rules.

As an adviser registered with the SEC, you have an obligation to comply with all of the applicable provisions of the Advisers Act and the rules that have been adopted by the SEC. This information sheet does not provide a complete description of all of the obligations of SEC-registered advisers under the law. To access the Advisers Act and rules and other information, visit the SEC's website at [www.sec.gov](http://www.sec.gov) (the Advisers Act and rules are available at <http://www.sec.gov/divisions/investment.shtml>).<sup>2</sup>

#### Investment Advisers Are Fiduciaries

As an investment adviser, you are a "fiduciary" to your advisory clients. This means that you have a fundamental obligation to act in the best interests of your clients and to provide investment advice in your clients' best interests. You owe your clients a duty of undivided loyalty and utmost good faith. You should not engage in any activity in conflict with the interest of any client, and you should take steps reasonably necessary to fulfill your obligations. You must employ reasonable care to avoid misleading clients and you must provide full and fair disclosure of all material facts to your clients and prospective clients. Generally, facts are "material" if a reasonable investor would consider them to be important. You must eliminate, or at least disclose, all conflicts of interest that might incline you — consciously or unconsciously — to render advice that is not disinterested. If you do not avoid a conflict of interest that could impact the impartiality of your advice, you must make full and frank disclosure of the conflict. You cannot use your clients' assets for your own benefit or the benefit of other clients, at least without client consent. Departure from this fiduciary standard may constitute "fraud" upon your clients (under [Section 206](#) of the Advisers Act).













#### Investment Advisers Must Have Compliance Programs

"You must employ reasonable care to avoid misleading clients and you must provide full and fair disclosure of all material facts to your clients and prospective clients....You must eliminate, or at least disclose, all conflicts of interest that might incline you — consciously or unconsciously — to render advice that is not disinterested. If you do not avoid a conflict of interest that could impact the impartiality of your advice, you must make full and frank disclosure of the conflict."

# Inaccurate, Omitted & Unclear ADV Disclosures Identified as a Risk by SEC Staff

**Risk Inventory Guide\***

This chart is intended to visually guide you through some of the risks that may be present as part of an adviser's everyday operations. As a CCO responsible for your firm's compliance, you should determine what risks are present and how they might affect your firm and its operations, assess whether the controls in place to manage or mitigate these risks are adequate, and make or recommend modifications to the compliance policies and procedures as necessary. You are not expected to personally perform all compliance-related activities. Rather, you "administer" or manage the compliance program by determining whether controls are necessary and what reviews and tests should be performed, when and by whom, and ensuring that business persons are involved in creating and complying with the established procedures. In essence, you determine "how much is enough."

	<b>Marketing/Performance:</b> • Inaccurate performance calculations • Overstated performance • Guarantees of profit • Unsubstantiated claims • Misrepresentation of services offered • Use of unapproved marketing materials • Misrepresentation about advisory firm and principals		<b>Objectives/Restrictions:</b> • Objectives not kept current • Objectives miscommunicated or not clearly understood • Adviser influences client to accept higher risk than desired • Failure to reconcile information communicated to portfolio manager and strategy implemented • Restrictions not monitored
	<b>Form ADV/Disclosures:</b> • Failure to provide Form ADV • Inaccurate, omitted, or unclear disclosures • Out of date disclosures • Misrepresentation of services offered • Failure to disclose potential conflicts of interest • Inaccurate account statements • Overstating account values		<b>Trade Ticket:</b> Preferential trade allocation • Side by side management conflicts • Investments outside client objectives or restrictions • Failure to include required information on trade ticket • Inappropriate allocation on partial fills
	<b>Invoices/Fees:</b> • Non-"research" products obtained without disclosure • Incorrect fee calculation • Use of inflated asset values • Direct debit of fees from custodial account • Prohibited fees		<b>Trade Execution:</b> • Failure to seek to obtain best execution • Favoring brokers based on research or referrals received • Post-trade allocation instructions • Principal or cross trades without required disclosure/consent • Errors/corrections not identified and resolved in client's best interest
	<b>IPO Offerings:</b> • Directing trades to brokers that provide IPO offerings • Placement of IPO allocations in adviser's proprietary or employees' personal accounts		<b>Non-public Information:</b> • Non public information obtained during analysis phase • Use of non-public information for personal gain/loss avoidance • Use of client trading to manipulate price of publicly traded stock
	<b>Soft Dollars/Kickbacks:</b> • Research and/or sources of research outside safe harbor • Inadequate due diligence on research product • Broker does not pay research source directly • Inaccurate or misleading research obtained • Research obtained is not current • Mixed-use items not appropriately allocated		<b>Personal and Proprietary Trading Account:</b> • Portfolio manager utilizes knowledge of upcoming trades for gain/loss avoidance in personal account • Trader uses knowledge of market and current or upcoming trades to manipulate prices or for gain/loss avoidance
	<b>Compensation:</b> • Incentive-based compensation leads to inappropriate recommendations or investments		<b>Money/Securities to/from Broker/Custodian:</b> • Funds or securities sent to the adviser or employees instead of the custodian • Theft

\* The Securities and Exchange Commission, as a matter of policy, disclaims responsibility for any private publication or statement by any of its staff. The views expressed by the staff in these written materials are those of the staff and do not necessarily reflect the views of the Commission or of other Commission staff.

The SEC's Risk Inventory Guide specifically identifies as operational risks: (a) inaccurate, omitted and unclear ADV disclosures; (b) out of date ADV disclosures; (c) misrepresentation of services offered; and (d) failure to disclose potential conflicts of interests.

## About Us

- ✓ Serve Over 500 Investment Advisor Firms
- ✓ Principals Are Industry Experienced Working in Compliance or Law Departments & Hold Professional Credentials
- ✓ Consult with Retail & Institutional Firms
- ✓ Offer Full Array of IA Compliance Services
- ✓ Reasonably Priced at Midwest Rates

RIA Compliance Consultants, Inc. is not a law firm and does not provide legal services.

# Work with Numerous IA Business Models

## Financial Planning

- Fixed
- Hourly
- Retainer

## Research Reports & Newsletter Subscriptions

## Solicitor

## Asset Management

- Discretion
- Non-Discretion

## Wrap Sponsor

## Third-Party Money Manager, Sub-Advisor and Signals Provider

## Fund Manager

- Private Fund
- Mutual Fund

# Our Turn-Key Service

Complete IARD Entitlement Forms

Act as IARD Service Bureau

Draft Custom Form ADV

Post Filings to IARD & CRD Accounts

Prepare Registration for Other States

Open Series 65 Window; File Waiver of Series 65 Due to Professional Designation (CFP, CFA & ChFC)

Draft Form U4

Advise of IARD Funding Requirements

Complete Miscellaneous Documents (Except Accounting)

Serve as Regulatory Liaison

Prepare Customized Written Compliance Policies and Procedures and a Code of Ethics

Provide a Packet of Sample Forms and Checklists to be Used to Help with Ongoing Compliance Responsibilities



## Consulting Fee for State Registration

- The consulting fee for our registration service is based upon a client's specific circumstances and anticipated advisory services.
- Please refer to our Consulting Agreement for the amount of the consulting fee and terms of such an engagement.

## Supervisory Procedures/Code of Ethics Our General Manual

- Firm Registration
  - IAR Licensing
- Fiduciary Duty
- Code of Ethics
  - Insider Trading
  - Personal Securities Transactions
  - Gifts and Entertainment
- Supervision
  - Outside Business Activities
  - Branch Office Audits
- Books & Records
- Client Documents and Disclosures
  - Conflicts of Interest
  - Annual ADV Offer
- Proxy Voting
- Custody
- Political Contributions
- Client Communications
  - Advertising,
  - Social Media & Networking Websites
- Advisory Services & Fees
  - Financial Planning
  - Asset Management
- Privacy
- Due Diligence
- Solicitor Arrangements
- Privacy
- Proxy Voting
- Trading
  - Errors
  - Allocations
  - Aggregation
  - Best Execution
  - Directed Trades
  - Discretion
  - Soft Dollar
  - Principal/Cross Trades
- Complaints & Investigations
- Business Continuity

## Supervisory Procedures/Code of Ethics Available Options

Regulator Specific,  
Template  
\$495

Self-Customized,  
Regulator Specific  
\$695

Regulator Specific,  
Customized  
\$1,295  
*3 Consulting Hours to  
assist with  
customization*

## Annual Compliance Program – Bronze Package

New CCO & Code of Ethics Webinars  
Compliance Webinars

Periodic Emails with General Compliance Reminders  
Sample Supervisory Forms

Compliance Manual Section Update Templates  
As-Needed Consulting (5 Hours)

IARD Renewal  
ADV Annual Amendment

**Fixed Consulting Fee \$240 per Month**

## Other Available Compliance Services

### Customized Compliance Program & Individual Services

Form ADV  
& Client  
Brochure

Solicitor  
Disclosure

Renewals &  
Annual  
Amendment

IARD  
Service  
Bureau

Supervisory  
Procedures  
& Code of  
Ethics

Privacy  
Policy

Section 13  
Filings

Advertising  
Reviews

Annual  
Review

Mock  
Regulatory  
Exam

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Melanie Howard – Ext 105

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# Thank You

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