

Financial Services Newsletter

Accounting and Reporting – 8 Best Practices for Investment Advisors

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The investment advisory business continues to grow more challenging. These best practices are designed to help your organization improve its accounting and reporting functions, mitigate risk, strengthen internal controls and safeguard client assets.

- **Review Your Middle and Back Office in Light of Your Strategic Direction.** The CFO, other senior financial executives and the General Partners (GPs) should hold reviews at least quarterly. When a holistic view is adopted and organized through a detailed and frank review process, you can determine whether the current middle and back office systems and internal controls are adequately supporting the organization's current and future needs.
- **Cyber Risk Assessments.** With more and more business conducted online, globally and via email, the risk of hacking and cyber theft has grown exponentially. Therefore, it is imperative to regularly test your systems to reduce the likelihood hackers will infiltrate. Regular assessments can identify system pitfalls and vulnerabilities and reduce the risk of cyber theft. Hackers routinely infiltrate company email systems, posing as a high ranking executive to illicitly request money transfers. They do this by monitoring executive emails, noting when the CEO or CFO travels. During that time, the hackers request an immediate wire transfer to meet an immediate deadline or solve an alleged problem. Fraud also arises relating to capital calls, distributions and drawdowns.
- **Implement Expense Allocation Policy and Procedures.** One of the SEC OCIE's (Office of Compliance Inspections and Examinations) ongoing areas of focus is expense allocation. When an SEC OCIE examiner visits your firm, they almost always review how you allocate expenses between the management company and the fund. And, if your investment advisor manages multiple funds, the inspectors review whether you have allocated expenses to the applicable fund that incurred the expense. It is important to establish and maintain a clear set of policies and procedures regarding expenses and allocation. To comply with SEC rules, it is critical to design expense categories (and general ledger codes) so your employees can properly allocate time and expenses (T&E) to enable accurate reporting and achieve compliance. If you conduct a "Mock SEC Exam," expense allocation should be an area of focus.
- **Budgeting, Forecasting, Performance Reporting and Analytics.** Preparing a budget and conducting a periodic review of revenue and expenses — especially in light of volatile investment markets — can help you identify gaps in resources, liquidity issues and calculate the GP's estimated tax payments. This can help you focus your management of the organization and achieve business goals and objectives.
- **Strengthen Internal Controls.** Conduct periodic reviews, ideally every three to six months and when there is a change in key personnel. Over time, we have observed lax controls surrounding employee turnover. Implement a set of protocols to be followed and a detailed checklist; for example, terminating former employees' access to the premises and systems immediately upon their resignation. During your review:
 - Analyze tasks and key functions against the personnel responsible for handling these tasks
 - Review the segregation of duties; for example, whether vendor onboarding, invoice approval and bill pay are handled by different employees.

Make changes and modifications as necessary and as your organization grows.

- **Tighten Control over Cash and Disbursements (and especially wire transfers).** Severely limit access to cash. Review the limits on single-signer authority. Spot-check and randomly review disbursements on a periodic basis. Implement a strict policy requiring dual-authentication and telephone approvals for wire transfers. Recently, while our team was working on a real estate transaction, we uncovered a hacker's email, which was a fraudulent attempt to reroute escrow payments to the hacker's bank.
- **Identify Tax Planning and Compliance Opportunities for GPs.** At least once a quarter (and in advance of material transactions and payment of incentives):
 - Meet with your tax department and advisors to explore tax planning opportunities
 - Review your organization's tax compliance and reporting requirements
 - Update your "punch list," noting reporting and filing deadlines

Since many investment advisors are organized as flow-through entities, there can be tax planning opportunities given the interrelationship between the GPs, the investment advisor and GP entities.

- **Review Your Policies and Procedures Manual.** Your organization's manual may be outdated given staff turnover and the way the business and technology has evolved. We find that many companies modify their business much more frequently than they update their policies and procedures manual. Make it a practice to review your manual quarterly and when there are significant developments in the business. Periodic reviews will enable the organization to update controls and identify necessary changes in business practices. This process also often prompts changes to streamline the accounting and reporting function and can ultimately reduce costs.

Contact Us

If you're an investment advisor, private equity firm, asset manager or other type of financial firm interested in streamlining your operations, improving your infrastructure or reducing operating costs, please contact the partner in charge of your account or the individuals below. PKF O'Connor Davies provides a comprehensive suite of what we call "Shared Support Resources" that you can leverage for some or all of your accounting functions.

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