**SEC’s 2025 Examination Priorities for Investment Advisers**

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On October 21, 2024, the U.S. Securities and Exchange Commission (SEC) Division of Examinations (the Division) released its annual [Examination Priorities](https://www.sec.gov/files/2025-exam-priorities.pdf) for fiscal year 2025 (the Report). The Report identifies certain critical risk areas where the Division may focus its resources in the upcoming year. Though the Report addresses risks applicable to a number of financial market participants, this Client Alert focuses on priorities relevant to SEC-registered investment advisers.

**Adherence to Fiduciary Standards of Conduct**

The Report first underlines the duties of care and loyalty that investment advisers owe to their clients. As fiduciaries, advisers must always serve the best interests of their clients and never place their own interests ahead of their clients’ interests. Advisers must also eliminate, or make full and fair disclosures of, conflicts of interest to ensure that they continue to render disinterested advice to their clients.

Specifically, the Division may focus on:

* Investment advice related to (1) high-cost products, (2) unconventional instruments, (3) illiquid and difficult-to-value assets, and (4) assets sensitive to higher interest rates or changing market conditions, including commercial real estate
* Dual registrants and advisers with affiliated broker-dealers by (1) assessing investment advice and recommendations regarding certain products to determine their suitability for clients’ advisory accounts, (2) reviewing disclosures made to clients regarding the capacity in which the recommendations are made, (3) determining whether account selection practices are appropriate, such as choosing whether to open a brokerage versus an advisory account, and (4) assessing whether such advisers mitigate and disclose conflicts of interest adequately and fairly
* How financial conflicts of interest may impact an adviser’s ability to provide impartial advice and best execution, especially in the context of nonstandard fee arrangements

**Effectiveness of Advisers’ Compliance Programs**

The Division continues to assess the effectiveness of advisers’ compliance programs pursuant to Rule 206(4)-7 under the Investment Advisers Act of 1940 (the Advisers Act), commonly known as the Compliance Rule. Under the Compliance Rule, SEC-registered investment advisers must (1) adopt and implement written policies and procedures that are reasonably designed to prevent violations of the Advisers Act, (2) designate a chief compliance officer responsible for administering such policies and procedures, and (3) review such policies and procedures at least annually for adequacy and effectiveness.

The Report notes that the Division typically focuses its examinations on “core” areas of advisers’ compliance programs, which include marketing, valuation, trading, portfolio management, disclosures and filings, and custody. Additionally, examinations typically include an analysis of the advisers’ annual reviews of the effectiveness of their compliance programs to address and monitor conflicts of interest, including those stemming from business and compensation arrangements, arbitration clauses, and party and transaction affiliations.

Examinations in 2025 may focus on:

* Fiduciary obligations of advisers that outsource investment selection and management
* Alternative sources of revenue or benefits that advisers receive, such as when advisers sell non-securities-based products to their clients
* Fee calculations and whether fee-related conflicts are disclosed in an appropriate and accurate manner

The Division may choose to further investigate any of these areas during a review of an adviser’s compliance program depending on the adviser’s practices or products. For example, advisers whose clients invest in illiquid or difficult-to-value assets, such as commercial real estate, may face higher scrutiny of their valuations of those assets. If advisers integrate artificial intelligence into their advisory operations, such as in portfolio management, trading, marketing, or compliance, examinations may look further into those advisers’ compliance policies and procedures, as well as their disclosures to clients related to those areas. Additionally, if advisers utilize independent contractors from geographically dispersed locations, examinations may focus on the advisers’ supervision and oversight practices. Advisers that are performing new services, that have recently made changes to their business models, or that are new to advising particular types of assets or clients may face examinations focusing on compliance practices.

**Examinations of Investment Advisers to Private Funds**

As a significant portion of the SEC-registered investment adviser population, advisers to private funds will continue to be subject to regular review. Specifically, the Division may prioritize reviewing:

* Disclosures to ensure that they are consistent with actual practices, including whether advisers have met their fiduciary obligations in times of market volatility and whether the private fund was exposed to interest rate fluctuations, as may be the case when the fund’s investment strategy involves commercial real estate, illiquid assets, or private credit. The Division may prioritize examinations of advisers to private funds that experienced poor performance and significant withdrawals or those that hold more leverage or difficult-to-value assets
* Accuracy of private fund fee and expense calculations and allocations at both the fund level and the investment level, with a focus on the valuation of illiquid assets, the calculation and offsetting of post-commitment period management fees, and the adequacy of disclosures
* Disclosures of conflicts of interest and risks, and the adequacy of related policies and procedures, especially in relation to products or practices that involve (1) the use of debt, fund-level lines of credit, investment allocations, adviser-led secondary transactions, or transactions between funds and others, (2) investments held by multiple funds, and (3) the use of affiliated service providers
* Compliance with recently adopted SEC rules, such as the 2023 and 2024 amendments to Form PF and the Marketing Rule

**Never Examined Advisers, Recently Registered Advisers, and Advisers Not Recently Examined**

In line with the [2024 Examination Priorities](https://www.sec.gov/files/2024-exam-priorities.pdf), the Division will continue prioritizing examinations of newly registered advisers and those advisers that have not recently or ever been examined.

**Our Thoughts**

The Report indicates that the SEC has continued to enhance its risk assessment capabilities, more recently by leveraging data and information to identify firms and practices that could present elevated levels of risk to investors and the markets. The Report states that the Division has hired skilled quantitative analysts and financial engineers to perform sophisticated data analytics in order to identify potential examination candidates and analyze large amounts of trade and other financial data. It appears that, as a result of these efforts, certain rule violations that previously may have gone unnoticed are now becoming easy targets of enforcement. In September 2024, for example, the SEC [levied penalties](https://www.sec.gov/newsroom/press-releases/2024-148) against various companies and individuals over failures to timely file information about securities holdings (through Schedules 13D and 13G) and public company stock transactions (through Forms 3, 4, and 5). The SEC indicated that it had relied on data analytics to identify these late filers. Thus, investment advisers should be aware of the SEC’s enhanced abilities to monitor and punish technical rule violations.

Consistent with reported priorities from recent years, the Division continues to emphasize that investment advisers must adhere to their fiduciary duties to clients. In 2019, when the SEC [clarified its position](https://www.lowenstein.com/news-insights/publications/client-alerts/sec-clarifies-federal-fiduciary-duties-of-investment-advisers-investment-management) on fiduciary duties with an [interpretation](https://www.sec.gov/rules/interp/2019/ia-5248.pdf) regarding standards of conduct, it emphasized that client sophistication and the scope of the advisory relationship affect the fiduciary duties owed to clients. Later, in the SEC’s [2023 adopting release](https://www.sec.gov/files/rules/final/2023/ia-6383.pdf) for the Private Fund Adviser Rules (PFARs), the SEC expressed that it maintained greater flexibility to interpret and enforce the fiduciary duties of private fund advisers. Among other examples, the SEC indicated that the inclusion of “hedge clauses” in advisory agreements and fund documents may conflict with those fiduciary duties.

Though the PFARs were ultimately struck down by the U.S. Court of Appeals for the Fifth Circuit on June 5, 2024, the SEC may still seek to prosecute advisers under the broad theory of fiduciary duty contemplated by the PFARs’ adopting release. As a preliminary example, in September 2024, the SEC [settled charges](https://www.sec.gov/files/litigation/admin/2024/ia-6672.pdf) with a private fund adviser for including hedge clauses in a private fund operating agreement that purported to irrevocably waive claims against the adviser for breaches of fiduciary duty on the basis that this clause was inconsistent with that fiduciary duty. As another example, again in September 2024, the SEC [charged an adviser](https://www.sec.gov/files/litigation/admin/2024/ia-6670.pdf) over the adviser’s informal practice of permitting certain fund investors to redeem their interests in the fund on shorter notice than what was stated in its policies on the basis that this practice was misleading to other investors. Advisers should be aware that the SEC may continue to bring enforcement actions over similar adviser behavior on the grounds that such behavior is misleading or in breach of fiduciary duties.

It is also noteworthy that many of the Report’s priorities are consistent with topics of enforcement actions that the SEC brought in 2024. For example, in [August](https://www.sec.gov/files/litigation/admin/2024/ia-6666.pdf) and again in [September](https://www.sec.gov/files/litigation/admin/2024/ia-6737.pdf), the SEC charged SEC-registered investment advisers for failing to implement policies and procedures reasonably designed to prevent the misuse of material nonpublic information (MNPI) related to the firms’ participation in ad hoc lender groups and creditors’ committees. Though the SEC did not allege insider trading in either action, it found that the firms’ policies failed to establish adequate procedures for monitoring or supervising firm personnel’s participation in such committees to prevent unauthorized receipt or use of MNPI. The SEC also brought a number of enforcement actions this year alleging violations of the Marketing Rule and failures to make appropriate disclosures or adequately address conflicts of interest, topics that are also highlighted in the Report as 2025 priorities.

Looking ahead to 2025, investment advisers should prioritize reviewing their policies and procedures regarding adhering to fiduciary duties and would be well advised to revisit provisions in fund governing documents that purport to waive, in whole or in part, the adviser’s fiduciary duties or specific obligations under the Advisers Act. Advisers should also take note of the Report’s reference to the Bank Secrecy Act of 1970, as amended (BSA), and the requirement that certain financial institutions establish anti-money laundering (AML) programs that are tailored to address the risks associated with the firm’s location, size, and activities. This is important considering that a new [Financial Crimes Enforcement Network rule](https://www.federalregister.gov/documents/2024/09/04/2024-19260/financial-crimes-enforcement-network-anti-money-launderingcountering-the-financing-of-terrorism), which goes into effect in January 2026, will subject investment advisers to the BSA and will require such advisers to implement AML programs, file suspicious activity reports, and comply with certain recordkeeping requirements. The Report indicates that the Division will continue to focus on AML programs. Thus, advisers would be well advised to implement any necessary changes to policies and procedures in 2025.

Finally, it is worth comparing the topics in the Report to the agenda for the [Compliance Outreach Program](https://www.sec.gov/compliance/complianceoutreach/compliance-outreach-program-national-seminar-agenda-110724) recently administered by the SEC on November 7, 2024. A number of the agenda items are consistent with the Report, such as adherence to fiduciary duties, accuracy of private fund fee and expense calculations, and compliance with the Marketing Rule. A number of other agenda items, such as off-channel communications, advisers’ oversight of third-party vendors, cybersecurity, and protection of investor information, could fall within the categories highlighted in the Report (e.g., adequacy of compliance policies and procedures) and are also likely to be a focus of the SEC’s examinations involving investment advisers in 2025.

Investment advisers should take note that the Report is not a comprehensive indicator of the issues that the Division may address during examinations. Lowenstein Sandler will monitor future publications from the Division and provide further updates in subsequent Client Alerts so that investment advisers can determine whether changes to their policies and procedures are necessary. Please reach out to one of the listed authors of this Client Alert or your regular Lowenstein Sandler contact if you have any questions regarding the Report.