



Analytical Note

To: Clients

From: Iron Road Partners

RE: Investment Adviser Off-Channel Case Identified in Examination

Date: 8/15/2024

Background:

- On August 14th 2024, the U.S. Securities and Exchange Commission (“SEC”) settled an administrative proceeding with 26 firms for off-channel communications. Only one of those firms was an investment adviser without also being registered as a broker dealer¹.
- This is the first enforcement case brought by the SEC where the off-channel communication was discovered during an SEC Examination.
- This investment adviser was charged with “failure to supervise” and violation of the Books and Records Rule. This investment adviser was not charged with Compliance Rule violations.
- While policies and procedures appeared to be in place, the SEC claims that insufficient policy surveillance was in place.

Key Facts and Allegations:

- **Books and Records**
 - **Policies and Procedures were in Place:** The SEC acknowledges that this investment adviser had sufficient off-channel communications policies and procedures. Employees were advised that the use of unapproved electronic communications methods was not permitted and acknowledged in writing that they read, understood, and abided by the adviser’s policies.
 - **Broad Policy Non-Compliance:** An SEC Examination identified off-channel communications issues which led to an Enforcement investigation. The adviser cooperated with the investigation and imaged employees’ phones to identify non-compliant individuals. The investigation revealed that off-channel communications were:
 - Sent and received internally and externally with clients, counterparties and other financial industry participants.
 - Books and Records Rule violations:
 - 204-2(a)(7)(i) : *triggered by discussing an investment strategy with a client.*
 - 204-2(a)(7)(iii): *triggered by the discussion of the placing or execution of orders.*

¹ In the Matter of P.Schoenfeld Asset Management LP; File No. 3-21999

Takeaways:

1. **Exam referral** – This is the first off-channel communication case that was brought by the SEC as a result of an exam referral. This case, therefore, could open the door to similar referrals and could embolden examiners to focus on off-channel communication issues in examinations.
2. **Broad definition of a required record** – This case broadly defines the violative conduct as not retaining communications sent *or* received. The OIP gave the example of an investment strategy communication with a client as having violated the Books and Records Rule’s requirement to retain communications *related* to investment advice given or proposed to be given. This reinforces most advisers’ approach to broadly prohibit off-channel communications for business purposes.
3. **Surveillance** – The OIP states that while policies and procedures were in place, the adviser did not have sufficient surveillance to ensure policy compliance. Given that off-channel technology solutions still have not matured, “lack of surveillance” could be an issue many advisers face.

Further Questions: Please contact us with any further questions at info@ironroadpartners.com