

RISK ASSESSMENT FOR INVESTMENT ADVISORS

In today's challenging regulatory and market environment, regulators and investors expect advisors to demonstrate that they have a strong risk management framework in place. The framework should provide for identification of potential risks, prioritization of those risks, development of internal controls to mitigate the risks, and documentation of policies and procedures for the ongoing monitoring and management of the risks. Berdon's risk assessment process provides a concise and cost-effective approach for identifying, scoring, and prioritizing risks specific to an advisor's business and risk profile.

The Berdon risk assessment process is designed to assist advisors in addressing the key categories of risk to a fund including operations and infrastructure, legal and compliance, liquidity, market, counterparty/credit and fraud, among others. The risks are aligned with the advisor's key business functions as well as broader regulatory and investor "hot points" such as corporate governance, "tone from the top," and demonstration of an effective "culture of compliance." As the risks are identified and prioritized, the advisor can drill down into the most critical risks and develop short- and long-term strategies to mitigate the risks. The process can be positioned as a key first step in validating or developing an enterprise risk management (ERM) program and/or a first phase in the development of a true risk-based internal audit plan.

The risk assessment process is quick and efficient and consists of a series of short phases to identify, prioritize, and manage those risks most critical to the funds. The process begins with facilitated sessions with management and key staff and then proceeds through a series of structured steps to further qualify and address inherent and residual risks. The final report highlights high, medium, and low risks with red, amber, and green designations and provides recommendations for developing strategies to mitigate the identified risks.

It has been our experience that this process helps the advisor focus in on those areas that could have the biggest impact on fund operations such as trade and investor allocations, movement of cash, alignment with agreements and limitations, valuations and Net Asset Value (NAV) processing, among others. Emerging risks as the investment profile of the advisor changes are also addressed, for example at the introduction of new strategies and managed funds.

Regulators and investors are increasingly looking for registered investment advisors to demonstrate that they have an ERM program in place as well as a strong internal audit function to ensure that necessary internal controls are ready and operating efficiently and effectively. In addition, the SEC has stated that they will prioritize examinations at registered advisors that exhibit certain risk characteristics and/or have not yet been examined, making it even more critical for the risk management functions to be an inherent and transparent component of the business.

The Berdon risk assessment process can serve as a dynamic tool to help identify, address, and monitor those risks that represent the most significant threats to the business.

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