



Deloitte & Touche LLP
695 East Main Street
Stamford, CT 06901-2141

Tel: +1 203 708 4000
Fax: +1 203 708 4797
www.deloitte.com

May 3, 2023

Ms. Vanessa A. Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street N.E.
Washington, DC 20549

Re: File Reference No. S7-04-23; Safeguarding Advisory Client Assets (SEC Release No. IA-6240)

Dear Ms. Countryman:

Deloitte & Touche LLP is pleased to respond to the request for public comment from the Securities and Exchange Commission (the "Commission") on the proposed rule, *Safeguarding Advisory Client Assets* (the "proposed rule" or "proposing release"). We appreciate the Commission's efforts to enhance protections of customer assets managed by investment advisers and therefore welcome the opportunity to share our observations on possible areas for clarification specific to the potential accounting and auditing implications of the proposal.

Scope of independent verification proposals

The proposed rule would require that an independent public accountant be engaged to perform certain examination or verification procedures for assets that are not held by a qualified custodian. If the Commission were to adopt these provisions, we believe further clarification of certain aspects of the proposed rule would be helpful, either directly in the final rule, or as guidance to supplement the Commission's 2009 guidance regarding accountant engagements performed pursuant to Rule 206(4)-2 of the Investment Advisers Act of 1940 (2009 Accounting Guidance).¹

For example, the proposed rule includes a requirement that an independent public accountant be engaged to perform a verification within one business day of any purchase, sale, or other transfer of beneficial ownership of securities or physical assets that are not maintained with a qualified custodian. We do not believe that, as proposed, such transactional verifications would be congruent with typical engagements under the current AICPA Professional Standards relating to attestations.² For example, an engagement under the attestation standards would require the independent public accountant to issue

¹ See SEC Release No IA-969, [Commission Guidance Regarding Independent Public Accountant Engagements Performed Pursuant to Rule 206\(4\)-2 Under the Investment Advisers Act of 1940](#).

² See AICPA Statements on Standards for Attestation Engagements (SSAE) No. 18, *Attestation Standards: Clarification and Recodification*. The four primary types of engagements are: assertion-based examination; direct examination; review; and agreed-upon procedures.

a written report upon completion of the engagement, which does not appear to be contemplated by the transactional verification provisions of the proposed rule. Additionally, we note that the Commission raised several alternatives to the proposed transactional verification provision in the proposing release. We encourage the Commission to consider whether one of those alternatives--such as verification on a quarterly or bi-annual basis, rather than verification on a transactional basis--might achieve the Commission's goals in a more efficient manner.

The Commission has also requested input on potential implementation challenges associated with the proposed requirement that during an annual examination an independent public accountant verify the existence and ownership of each of the client's privately offered securities or physical assets that are not maintained with a qualified custodian. The Commission may want to consider clarifying that it would allow for sampling to fulfill this requirement, and that verification of each asset would not be necessary.

Additionally, the proposed rule would define "assets" to include funds, securities, or other positions held in the client's account. The proposing release clarifies that the term "other positions" would include physical assets (such as artwork, real estate, precious metals, or physical commodities) and digital assets. Not all independent public accountants have the specific expertise or resources necessary to verify such a wide variety of assets. Because of this, there may be limitations on the availability of independent public accountants to perform such services. Further, the digital asset space is still developing and newly-created digital assets may emerge prior to the development of a qualified custodian to hold them. We believe it would be helpful for the Commission to identify a transition plan for investment advisers whose clients may wish to invest in such digital assets for which a qualified custodian does not yet exist and provide guidance to independent accountants engaged to perform security counts or audits under the proposed rule.

The annual audit exemption

The proposed rule allows for exemption from certain requirements when the entity is subject to an annual financial statement audit that meets specific regulatory requirements, including that the audited financial statements are prepared in accordance with U.S. Generally Accepted Accounting Principles ("U.S. GAAP") or, for certain entities, contain information substantially similar to statements prepared in accordance with U.S. GAAP and material differences with U.S. GAAP are reconciled. We encourage the Commission to consider the current requirements in local jurisdictions that may require financial statements to be prepared under a different basis of accounting. In some instances, the requirement to prepare U.S. GAAP, or substantially similar, financial statements may require an adviser and their investors to incur additional costs to prepare and have audited financial statements on two different bases of accounting, especially if auditors in those jurisdictions conclude that including a reconciliation is not in conformity with the required basis of accounting. The Commission may wish to consider whether certain recognized bases of accounting, including, but not limited to the International Financial Reporting Standards, might be sufficient on their own without also requiring U.S. GAAP financial statements or financials with a reconciliation to U.S. GAAP.

Internal control report provision

The proposed rule would require that a written agreement with the qualified custodian regarding the possession or control of client assets must provide that the qualified custodian, at least annually, provide a written internal control report that includes an opinion of an independent public accountant "as to whether controls have been placed in operation as of a specific date, are suitably designed, and are operating effectively to meet control objectives relating to custodial services." We agree with the

Commission that an effective internal control environment provides valuable investor benefits and protections.

The proposing release notes the Commission intentionally did not require the provision of a specific type of internal control report, in order to allow for flexibility in meeting the regulatory requirements. While we appreciate the Commission's desire for flexibility, we think it would be helpful if the Commission would clarify its expectations when the investment adviser is also the qualified custodian. The proposed rule states, "[i]f you are the qualified custodian, or if the qualified custodian is a related person, the independent public accountant that prepares the internal control report must verify that client assets are reconciled to a custodian other than you or your related person...." The Commission may consider clarifying whether the intent of this requirement is that the independent public accountant test the effectiveness of reconciliation controls, or whether it intends that the independent public accountant would perform a separate engagement to perform more attestation-like verification procedures by comparing the records of the qualified custodian with those of the unaffiliated party, which might include confirmation procedures. If verification procedures are expected, we believe it would be helpful if the Commission were to confirm that the independent public accountant may perform testing on a sample basis and may perform such testing either throughout the period or at a point in time. Moreover, because some custodians hold the assets of numerous different entities, performing testing that covers holdings from each entity could result in unnecessarily large sample sizes; we therefore recommend the Commission clarify that verification procedures would not be required to cover assets from each entity whose assets the custodian holds.

* * * *

We appreciate the opportunity to provide our perspectives on the current proposal. If you have any questions or would like to discuss our views further, please contact Rajan Chari at (312) 486-4845.

Sincerely,

A handwritten signature in cursive script that reads "Deloitte & Touche LLP".

Deloitte & Touche LLP