Russia-Ukraine war

The impact of the Russian government’s invasion of Ukraine is highly uncertain and impacting business globally—including the asset management industry. For our industry, it is important to consider the impact of service provider operations, investment exposures, and decisions. Direct and indirect implications should be considered. For instance, while a service provider may not have operations directly impacted, it is possible that key personnel at service providers are personally affected, which may in turn impact their ability to fulfill their responsibilities.

Our recommendation: Ask questions to understand whether management has a good understanding of the direct and indirect implications and what they are doing to assess and react to the resulting risks. As the situation continues to evolve, understand the risk assessment and monitoring mechanisms in place and how they are being deployed.

Areas of focus for directors:
- To what extent are operations and personnel impacted?
- Are there stresses impacting the effectiveness or efficiency of operations?
- Is there direct exposure to the funds and investor communication strategy?
- Is there any indirect impact to the funds and what is being done to manage the indirect risks?
- What is the market liquidity for Russian and Ukrainian securities, and how is liquidity being managed?
- What is the impact on the valuation of investments and is the pricing reliable?
- Are there any debt securities that are showing signs of default or likely default because of the current situation? What is being done to assess valuation and collectability of interest?

For additional information and insights on how to help navigate uncertainty amid the Russia-Ukraine war, visit our website: https://www.kpmg.us/insights/2022/ukraine-response-hub.html.

Digital transformation

This year marks the third year of asset managers virtually interacting with their clients. This shift to the virtual was not wholly unexpected pre-COVID-19, but what we thought would take years to implement happened almost overnight. This change has been profound for the industry and has accentuated the need for digital transformation. More importantly, asset managers not only successfully adapted to transformative change but also are in fact...
benefitting from this new way of working. Our “2021 CEO Outlook” survey further validates that digital transformation is a priority for over 75 percent of asset management CEOs.

Areas of focus for directors:
— How are management and key service providers investing in and transforming their business using technology? This includes investment operations, fund accounting, transfer agency, custody, fund administration, and investor connectivity.
— How will transformation benefit investors?
— What risks have or will arise because of the efforts and how are they being managed?

For more information, read our newest blog from Kalpana Ramakrishnan, Financial Services Advisory leader at KPMG in the U.S.: https://www.linkedin.com/pulse/three-steps-asset-managers-maximize-benefits-from-ramakrishnan/?published=t.

Environmental, social, and governance (ESG)
ESG considerations are important to investors, market participants, and regulators. ESG is driving new funds and altering others. Of course, regulators are concerned with whether ESG assertions are appropriately supported by process and actions and not merely hyperbole.

Areas of focus for directors:
— What is the role of ESG in each of the funds?
— What are the expectations for new funds?
— How is ESG being marketed to investors?
— What is the adviser’s process and rigor to ensure that assertions are adequately understood and supported by action that is actively monitored?
— What is the degree of expertise by the adviser and service providers that enable this activity?

Crypto assets
Many advisers are thinking about how to add crypto assets into the investment mix. The U.S. Securities and Exchange Commission (SEC) has heightened interest in direct investments in crypto assets due to custodial and valuation concerns. As a result, there is very little direct investment in crypto by 1940 Act funds, and this will continue until these issues are addressed to the SEC’s satisfaction. However, indirect investment in such assets using derivative financial instruments has occurred. But there are concerns about the size of market for such instruments and the resulting liquidity in those markets.

Areas of focus for directors:
— Are managers thinking about adding new crypto asset funds or adding exposure to crypto assets with existing funds?
— How will custody, valuation, and liquidity be monitored and managed?
— What is the degree of expertise by the adviser and service providers that enable this activity?

Less-liquid investments
As funds search for ways to deliver returns, less-liquid investments in the form of private equity, venture capital, private credit, and less-liquid real estate positions are being added using newly formed closed-end funds and by adding such positions to existing funds. Inherently, valuation of such investments is more subjective and liquidity of such positions is typically less.

Areas of focus for directors:
— Do the advisers plan to add less-liquid investments through new funds or by adding exposure in existing funds?
— How will such investments be valued? What is the frequency and will service providers be utilized?
— How are any liquidity differences between the investments and the fund’s obligations to investors being identified and managed?
— What is the degree of expertise by the adviser and service providers that enable this activity?
— How will calibration and back testing be employed in the valuation process?

Cybersecurity
In the world of digital interconnectivity, cybersecurity is inherently critical. Cybersecurity is constantly changing as new threats and deterrents are continuously emerging. In response to this, the SEC has proposed rules that would be applicable to advisers and funds that would bring more clarity around responsibilities while increasing reporting obligations.

Areas of focus for directors:
— What are the advisers and service providers’ cybersecurity programs, testing, event identification, and reporting plans/capabilities?
— What is their insurance coverages for cyber incidents? What is covered and what is not?
From the insurer, what are the top reasons cyber incident claims are rejected? What are the adviser and others are doing to manage that risk?

What is the degree of cybersecurity experience by the adviser and key service providers?

### Talent management

Globally, knowledge workers (i.e., finance, investment, and accounting professionals) are in shorter supply due to pandemic-related and demographic-related changes and challenges. These shortages impact quality and cost and are resulting in an increased focus on and pace of digital transformation efforts of investment operations, fund accounting, and fund administration.

### Areas of focus for directors:

- What are the pressures being faced from each of your key service providers and how are they being addressed?
- How are labor costs being impacted to manage any stresses?
- How are the use and management of outsourcing and automated solutions helping to mitigate the risks?
- What challenges and opportunities are available now with a hybrid work environment? How are your service providers addressing hybrid work?

### KPMG can help

We would like to hear from you on how these issues are impacting your business.

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