



**Risk Management Update
November 2015**

COMPLIANCE END-OF-YEAR CHECKLIST UPDATE

On November 18, 2015, SEC Chair Mary Jo White gave testimony to the Committee on Financial Services, outlining the various steps the SEC has been taking and what they plan on doing going forward in regards to the financial markets and financial services industry.

Chair White informed the Committee that the SEC's enforcement program "continued to deliver very strong results," which totaled to 807 enforcement actions with sanctions of \$4.2 billion for the 2015 fiscal year. Among the 807 actions, there were a number of "first-ever" cases.¹

In addition, Ms. White spoke about the initiatives currently being considered for investment advisers and investment companies, stating the following:

"At my direction, the SEC staff is working on additional initiatives aimed at helping to ensure the Commission's regulatory program is fully addressing the increasingly complex portfolio composition and operations of the asset management industry. These initiatives include:

- ***Use of Derivatives by Investment Companies.*** SEC staff is working on recommendations to the Commission to propose new requirements related to the use of derivatives by registered funds, including measures to appropriately limit the leverage these instruments may create and enhance risk management programs for such activities.
- ***Transition Plans for Investment Advisers.*** Staff is also developing recommendations for the Commission to propose requiring investment advisers registered with the Commission to create and maintain transition plans to prepare for a major disruption in their business.
- ***Stress Testing for Large Investment Advisers and Large Investment Companies.*** Staff is also considering recommending that the Commission propose new requirements for stress testing by large investment advisers and large investment companies. Such rules would implement in part requirements under section 165(i) of the Dodd Frank Act.
- ***Third-Party Compliance Reviews.*** At my direction, staff is also preparing a recommendation to the Commission for proposed rules requiring third-party compliance reviews for registered investment advisers. The reviews would not replace examinations conducted by our Office of Compliance Inspections and Examinations, but would be designed to improve overall compliance by registered investment advisers."

¹ See <http://www.sec.gov/news/pressrelease/2015-245.html>.

In light of the above, this month's Risk Management Update provides an end-of-year checklist that imparts important tasks covering required compliance filings, along with conflict and risk mitigation steps for consideration by compliance personnel. Importantly, this list is not all inclusive, and firms should consider their business practices in light of regulations, recent enforcement actions, and SEC initiatives to determine if additional steps are necessary.

Compliance Checklist:

- Confirm the firm's IARD annual filing fees are paid within the required deadline. (*Useful tip:* This year's deadline is December 18th and if you are paying by check, it should be mailed early to allow for time for FINRA processing.)
- Review the firm's policies and procedures manual to ensure the underlining policies and procedures clearly reflect current business activities and include applicable required state and federal regulations. (*Useful tip:* Document your findings as part of the firm's annual review and communicate all changes to senior management and firm personnel.)
- Ensure all necessary compliance steps outlined in your firm's policies and procedures have been performed (or will be by end of the year), including annual testing, compliance risk assessments, regulatory filings, branch office audits and supervisory reviews. (*Useful tip:* Consider utilizing compliance software that prioritizes and provides an audit trail of what has been review, by whom and when.)
- Confirm annual delivery of the firm's privacy notice to all clients, and review the effectiveness of safeguarding protocols to protect confidential, non-public client information. (*Useful tip:* Consider the Risk Alerts and Interpretive Guidance issued by the SEC on cybersecurity.²)
- Ensure that all annual compliance reporting has been completed by supervised persons, including but not limited to reports covering annual securities holdings, outside business activities, political contributions, gifts and entertainment. (*Useful tip:* Consider using third-party compliance software to facilitate the reporting and annual certification process and evaluate responses for new conflicts that require disclosures to clients and investors.)
- Confirm with registered personnel that their currently filed Form U-4 contains update and accurate information. (*Useful tip:* Distribute a current copy of the filed Form U-4 to each registered supervised person for review.)
- Ensure that applicable required federal and/or state filings have been made, including state net capital filings, state registrations, state notice filings, Form 13-F, Schedule 13-D/G, Form 13H, Form PF, Form D (private funds), and state blue sky filings. (*Useful tip:* To maximize efficiencies, consider software and third-party outsourcing solutions to assist with these filings.)
- For private funds, verify that the annual audit of the fund's financials is scheduled, and that internal controls are in place to ensure mailing of the audited financial statements to investors within the required time period. (*Useful tip:* Coordinate with the Fund's third-

² See OCIE, NEP Risk Alert, OCIE Cybersecurity Initiative (Apr. 15, 2014) available at <https://www.sec.gov/ocie/announcement/Cybersecurity-Risk-Alert--Appendix---4.15.14.pdf> and OCIE Examination Priorities for 2015 (Jan. 13, 2015) available at <http://www.sec.gov/about/offices/ocie/national-examination-program-priorities-2015.pdf> and OCIE, NEP Risk Alert, Cybersecurity Examination Sweep Summary (Feb. 3, 2015) available at <https://www.sec.gov/about/offices/ocie/cybersecurity-examination-sweep-summary.pdf> and OCIE, NEP Risk Alert, OCIE's 2015 Cybersecurity Examination Initiative (Sep. 15, 2015) available at <https://www.sec.gov/ocie/announcement/ocie-2015-cybersecurity-examination-initiative.pdf>.

party service providers and employees to allow sufficient time to prepare and facilitate the audit.)

- Review current registration documents and client disclosure documents (such as Form BD, Form N1-A, Form ADV Parts 1, 2A and 2B, client agreements, and private placement memorandums) to ensure they reflect current information and contain all required disclosures. (*Useful tip:* Read the SEC issued instructions for the document to ensure you are including all required information.)
- Review standard client agreement(s) for clear and concise delineation of roles and responsibilities of the parties and servicing mandates. (*Useful tip:* It is important to have legal counsel review all standard agreements to help protect the firm from unnecessary liabilities, particularly as the business model evolves.)
- Ensure that business websites, social media sites, presentations, commentaries, and other marketing materials are up-to-date, contain all necessary disclosures, have been reviewed by compliance, and copies are retained as required. (*Useful tip:* Perform testing to confirm that the firm is only using currently approved marketing and promotional materials.)
- Analyze maintenance and safeguarding controls for firm required books and records, including client, corporate and financial records. (*Useful tip:* Utilize a spreadsheet to identify and document required records, controls already in place, and those persons responsible for maintenance.)
- Review and test the firm's business continuity plan, including cybersecurity protocols, to ensure adequate controls are in place for back-up and restoring electronic data, cybersecurity preparedness, and adequacy and responsiveness of redundancy sites. (*Useful tip:* Provide periodic training to supervised persons covering the firm's plan, including current cyber-crimes and what to do in cases of identified threats.)
- Audit client files to ensure that investment objectives have been documented and are current. (*Useful tip:* Consider automating "new account" intake process to help ensure timely receipt of required new account documentation.)
- Review solicitor arrangements to verify that agreements are up-to-date and in compliance with Rule 206(4)-3 of the Advisers Act, and solicited clients received a copy of the solicitor's disclosure statement. (*Useful tip:* Obtain annual written representations from each solicitor that they are still in good standing and are adhering to requirements under agreement.)
- Review surveillance reports, exception reports, and checklists for detection of trends and patterns indicating systemic risk areas and take appropriate actions as needed. (*Useful tip:* Use technology to the extent possible to perform trend analysis reviews and document all results.)
- Confirm that due diligence reviews have been performed on critical service providers, third-party managers and investments. (*Useful tip:* Send annual questionnaires and obtain and review various documents such as financial statements, written policies and procedures, business continuity plans, public regulatory filings, privacy safeguards, SSAE 16 reports and other internal control documents.)
- Ensure compliance training has been provided to firm personnel, particularly as it relates to required reporting by supervised persons, new and revised firm policies and procedures, and risk and conflict areas. (*Useful tip:* Consider using webinars, lunch and learn compliance presentations, and periodic compliance emails to assist in educating.)

Conclusion

In addition to getting prepared for year end, firms should be considering their budget and compliance resources for 2016 and beyond. The initiatives the SEC are looking to propose will have a definite cost impact on firms that needs to be proactively contemplated. Further, it is important to consider how technology can assist with lessening the administrative burden and free up human resources.

To find out about technology solutions offered by CCLS and how we can further assist with year-end compliance planning and beyond, please contact us at info@corecls.com, at (619) 278-0020 or visit us at www.corecls.com for more information.

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