



Risk Management Update September 2010

SUCCESSION PLANNING: A CRITICAL COMPONENT TO YOUR BUSINESS CONTINUITY PLAN

You arrive at work at 8am Monday morning to learn your CEO is in the hospital after suffering a head injury while skiing over the weekend. Doctors speculate the CEO will require 10-12 months of rest and intensive rehabilitation. You can't help but wonder: "How will my company survive without its Commander in Chief?"

For many businesses engaged in the financial industry, this type of disrupting event could cause the downfall of the firm, particularly if the CEO is the primary rainmaker. In other firms, the CEO also may be the star Portfolio Manager and there is no alternate individual who has quite the same skill set. For this reason, having a viable Succession Plan is essential to the health of the firm and provides for necessary internal controls to help instill client confidences in placing investments with that firm.

Succession Planning for the Future

Succession planning involves identification and development of key personnel who would fill the key leadership positions in a firm. Best practices for a working Succession Plan combine both of these elements, forming a parachute for the firm should an unexpected event occur.

Identification of Personnel

Identifying and assessing potential candidates within a firm is the first step in the implementation of a working Succession Plan. Important to the identification process is the careful definition of what competencies are required for each key position at the organization. Essential characteristics and competencies should be identified and mapped to those individuals who may fit the criteria. If no such person is found internally, consider external sources (such as colleagues within the financial industry) as a potential successor.

Individual Development

After identifying potential successors, it is important to provide training to help ensure proper development of the skill set necessary to carry forth business operations. Such development may include, but is not limited to the following:

- Understanding of the organization's long term goals and objectives
- Education on competencies and other needed criteria
- Understanding of personnel goals both short term and long

During this stage, it is essential to discuss the firm's short- and long-term goals, and how they may evolve as technologies, the economy and personnel change. Having this working understanding of these visions for the firm should enable the successor to strategically implement new directions where appropriate.

The Business Continuity Plan

A viable Succession Plan will compliment the firm's Business Continuity Plan ("BCP") as a whole. Investment Advisory firms are required under SEC guidelines to maintain policies and procedures which detail emergency planning as well as guidelines for succession operations. For guidance in this area, FINRA promulgated Rule 4370, which requires its member firms to implement a written business continuity plan which addresses (at a minimum) the following areas:

1. Data back-up and recovery (both hard copy and electronic);
2. Mission critical systems;
3. Financial and operational assessments;
4. Alternate communications between customers and the member;
5. Alternate communications between the member and its employer;
6. Alternate physical location of the employees;
7. Critical business constituent, bank and counter-party impact;
8. Regulatory reporting;
9. Communications with regulators; and
10. Assuring customers will have prompt access to their funds/securities in the event the member is unable to continue business.

For more information on formation of the business continuity plan or for a small firm template for BCP, please visit www.finra.org/Industry/Issues/BusinessContinuity/p006464.

Additional Succession Plan Considerations

As part of the requirements under FINRA Rule 4370, firms must disclose to customers at account opening, how its BCP and Succession Plan will allow the firm to continue its operations should there be a significant business disruption.

Often times financial institutions focus on operational recovery and do not address human capital. For smaller firms, consider like or similarly situated businesses which can serve not only as an alternate location or operational solution in the case of a disaster, but also could provide a resource for identifying potential professionals who could serve as a successor should something happens to the business owner.

When implementing a Succession Plan, consider the following:

1. Do key firm personnel have enough information to know what to do if something happens to the owner?
2. Is there a draft communication to clients to let them know what to expect in the owner's absence?
3. Has the firm prepared a response to client inquiries on who will run the firm in the owner's absence?
4. Does the owner's family know what to do in the "what if" scenario?

Taking steps to formulate a Succession Plan now will help strengthen internal controls and prevent chaos if an unforeseen event ever occurs. For more information please do not hesitate to contact us at (619) 278-0020.

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