



**Risk Management Update
October 2014**

COMPLIANCE END-OF-YEAR CHECKLIST UPDATE

The upsurge in regulatory oversight, new data and analytical tools available to regulators and heightened scrutiny of the financial services industry by state and federal regulators in 2014, are demanding more time and resources of compliance professionals to keep pace with the never-ending regulatory environment.

True to a speech delivered last year at the Securities Enforcement Forum,¹ Securities and Exchange Commission (“SEC”) Chairman Mary Jo White continues to take a strict and unyielding approach to the enforcement of federal securities laws. Noteworthy is the unprecedented enforcement cases brought this year by the SEC. In the preliminary report for the fiscal year ending in September, the SEC released their findings which show a record 755 enforcement actions brought in 2014, up substantially over the same time period last year.²

The SEC’s Office of Compliance Inspections and Examinations (“OCIE”) has been busy this year with several examination initiatives, some of which are noted below pertaining to investment advisers, broker-dealers, hedge funds, private equity firms, municipal advisers, and other SEC-regulated firms, including:

- Limited scope examination of never-before examined registered investment advisers;
- Examination of more than 50 registered broker-dealers and registered investment advisers focusing on cybersecurity governance and assessment of cybersecurity risks;
- Continuation of Presence examinations to help identify high risk areas of private equity firms not present in other adviser business models for detection of violation of securities laws; and
- Focused examinations on municipal advisors that are newly registered under the SEC’s final Municipal Advisor Rule which went into effect on July 1, 2014.³

This month’s Risk Management Update provides an end-of-year checklist designed to address higher risk areas that should be performed by year-end. While this list is not all inclusive, given the pulse of heightened regulatory requirements, it can provide a foundation to your firm’s internal control assessment.

- Review current registration documents and client disclosure documents (such as Form BD, Form ADV Parts 1, 2A and 2B, contracts and private placement memorandums) to ensure they reflect current information and contain all required disclosures. (*Helpful hint: Be sure to reflect new business lines, change in ownership, conflicts of interest, and other important disclosures, as applicable.*)

¹ See http://www.sec.gov/News/Speech/Detail/Speech/1370539872100#.VEq_svnF9nY.

² See <http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370543184660#.VErAffnF9nY>.

³ See <http://www.sec.gov/rules/final/2013/34-70462.pdf>.

- Review standard client agreement(s) for clear and concise delineation of roles and responsibilities of the parties and servicing mandates. *(Helpful hint: It's important to have legal counsel review all standard agreements to help protect the firm from unnecessary liabilities, particularly as the business model evolves.)*
- Determine whether your firm's compliance Policies and Procedures Manual clearly reflects your business, particularly due to change in business practices and/or regulatory framework. *(Helpful hint: Document your findings as part of the firm's annual review and communicate all changes to senior management and firm personnel.)*
- Analyze maintenance and safeguarding controls for required books and records, including client, corporate and financial records. *(Helpful hint: Consider electronic retention of required books and records or 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 procedures, to ensure adequate controls are in place for back-up and restoring electronic data, cybersecurity preparedness, and adequacy and responsiveness of redundancy sites. *(Helpful hint: Reference the SEC's National Examination Program Risk Alert of April 15, 2014 for OCIE's Cybersecurity Initiative on addressing cyber threats.)*
- Check client files to ensure that investment guidelines have been documented and are current. *(Helpful hint: Consider automating "new account" intake process to help ensure timely receipt of required new account documentation.)*
- 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. *(Helpful hint: Review the firm's current Regulation S-P, Regulation S-ID and Business Continuity Plan internal controls and enlist the assistance of IT personnel to test current safeguarding effectiveness.)*
- Ensure that your website, social media sites, pitch books, and other marketing materials are up-to-date, contain all necessary disclosures and are timely reviewed and retained as required. *(Helpful hint: Confirm only currently approved marketing and promotional materials are being used by sales and marketing personnel.)*
- Review solicitor arrangements to verify that agreements are up-to-date and in compliance with Rule 206(4)-3 of the Advisers Act, and clients are receiving a copy of the solicitor's disclosure statement. *(Helpful hint: Perform a background check on solicitors to ensure that they are still in good standing.)*
- Review surveillance reports, exception reports, and checklists for detection of trends and patterns indicating systemic risk areas and take appropriate actions as needed. *(Helpful hint: Use technology to the extent possible to perform trend analysis reviews and document all results.)*
- Perform diligence reviews on critical service providers, third-party managers and investments. *(Helpful hint: Send annual questionnaires and obtain and request documents such as financial statements, business continuity plans, regulatory filings, privacy safeguards, SSAE 16 reports and other internal control documents for review.)*
- Review what compliance training has been provided to firm personnel, particularly as it relates to identified compliance infractions and newly implemented policies and procedures, and conduct additional training, as needed. *(Helpful hint: Consider using*

webinars, lunch and learn presentations, and periodic compliance email reminders to assist in educating and updating firm personnel.)

- Ensure that all annual compliance documents have been received from personnel (such as disclosures involving outside business activities, political contributions, gifts and entertainment, and personal trading. *(Helpful hint: 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 Form U-4 contains current and accurate information. *(Helpful hint: Distribute to registered personnel a current copy of their Form U-4 for review and amendment.)*
- Consider whether all necessary compliance reviews and steps set forth in the firm's policies and procedures manual have been performed, including annual testing, periodic risk assessments, regulatory filings, branch office audits and supervisory reviews. *(Helpful hint: Consider utilizing compliance software that prioritizes and provides an audit trail of what has been review, by whom and when.)*
- Ensure that applicable required federal and/or state filings have been made, including net capital filings, notice filings, Form 13-F, Schedule 13-D/G, Form 13H, Form PF, Form D and Blue Sky (state) filings, as applicable. *(Helpful hint: 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. *(Helpful hint: Coordinate with the Fund's third-party service providers and employees to allow sufficient time to prepare and facilitate the audit.)*

Conclusion

Overseeing and advancing a firm's compliance program is a continuous process that demands critical attention of compliance personnel and senior management. An end-of-year checklist, coupled with technology solutions, can provide an efficient, cost-effective means to assist with monitoring and maintenance of your compliance program.

To learn more about technology solutions offered by CCLS and for additional considerations for your compliance program, including essential end-of-the-year assessments, 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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