complinet

Article

Tracker impact analysis: SEC warning to registrant CEOs: now is not the time to neglect compliance

MAYER • BROWN

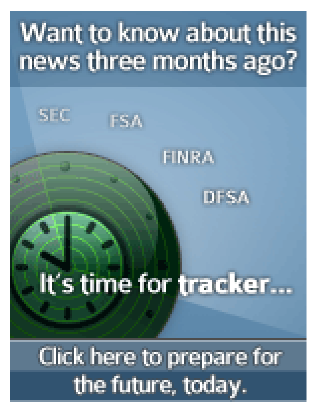
Jan 08 2009 Jeffrey F. Robertson and Akrivi Mazarakis

Jeffrey F. Robertson and Akrivi Mazarakis

Facing an unprecedented global economic crisis, businesses naturally are exploring ways to cut costs. In doing so, SEC registrants — investment advisers, investment companies and broker-dealers — should not compromise their compliance and risk management programs.

In a recent letter addressed to registrants' CEOs and posted on the SEC's Office of Compliance Inspections and Examinations (OCIE) website, OCIE director Lori Richards reminded CEOs of their firms' "legal obligation to maintain an adequate compliance program reasonably designed to achieve compliance with the law." The letter came on the heels of a similar message that SEC Chairman Christopher Cox conveyed to chief compliance officers attending the SEC's national CCOutreach seminar last month. Chairman Cox cautioned that "[w]hen a company cuts compliance, violations will occur. And if violations occur, punitive actions should and will be taken . . . There will be no favor granted because a company made a cost-cutting decision to minimize [its] compliance budget." Similarly, the FSA warned in its 2008 Financial Risk Outlook that increased financial pressures could distract companies from their usual risk-management processes.

The SEC stressed, in addition to its usual audience of chief compliance officers, the importance of registrants developing a pervasive "culture of compliance" from the highest executive to the lowest-level employee. While the warning could not be clearer, it begs the question — just how do registrants ensure that their compliance programs are up to snuff? Below are a few tips for registrants to maintain effective compliance programs.



Develop a culture of compliance

Whether a firm possesses a culture of compliance is a subjective assessment. However, certain guideposts may help firms predict how regulators may view them in this respect.

For example, whether compliance staff has the resources and authority and/or discretion to permit them to effectively carry out their responsibilities is key. Likewise, compliance staff access to the various activities of the firm; employees' responsiveness to compliance requests; and how frequently employees consult compliance for guidance on particular issues are all important factors.

A culture of compliance requires top management to reinforce its importance. Senior management sets a positive example when it consults with compliance before making key business decisions — to assess the regulatory impact of those decisions and to allow compliance to address potential effects of those decisions on compliance efforts.

Undertake proactive & periodic risk assessment

No one understands the unique risks that may affect a particular registrant more than the registrant itself. So it is important that compliance staff periodically assess the risks that affect the firm's business model — especially given the constant evolving financial and regulatory landscapes. As new risks are identified, viable solutions should be developed and implemented. The absence of a perfect solution to a particular problem does not excuse inaction in the regulators' eyes. After all, registrants are obligated to implement compliance programs that are reasonably designed, not perfectly designed, to achieve compliance with relevant laws and regulations.

Monitor regulatory trends and deficiencies

In addition to risk assessment, maintaining an effective compliance program requires firms to identify new regulatory trends and to learn from others' mistakes. Monitoring SEC and FINRA websites can go a long way in these respects. In the last few years, the OCIE has greatly increased its transparency by remaking its website into a useful guide for registrants seeking to improve their compliance programs. The site includes special reports and studies, key speeches, a comprehensive anti-money laundering guide, "Compliance Alerts," tips for newly registered investment advisers, and descriptions of the examination process. The "Compliance Alerts" summarize the most common deficiencies for each type of registrant based on prior examinations. These deficiencies provide a useful roadmap for self-evaluation and improvement. Just recently, the OCIE added a "core initial" request for information from investment advisers, which seeks to increase transparency and standardize across all SEC regional offices the format of the initial document request sent to investment advisers when beginning an examination.

To the extent possible, having compliance staff attend conferences where the SEC, FINRA, or other regulators speak is also useful. Whether through the CCOutreach program or industry working groups, there is great value in learning about compliance programs and experiences of peer firms by speaking directly with compliance staff of similarly situated firms.

Re-examine compliance programs

As the substance of compliance efforts changes so must the structure. Registrants should re-examine their compliance program, including key areas identified below, to evaluate the strength of each in light of newly identified risks.

Policies and procedures — Periodically, registrants must assess their policies and procedures to ensure that they are comprehensive and accurately reflect established practices within the firm. This includes both supervisory procedures as well as department-specific procedures. Registrants should update procedures to reflect staffing changes and ensure that supervisors' functions are adequately established and documented.

Training — Registrants should conduct training programs for new employees regarding both their specific responsibilities and issues that extend beyond their job title, such as detecting and reporting suspicious activity and guarding against the misuse of non-public information. Firm-wide continuing education to existing employees will help employees stay abreast of new issues affecting how they carry out their specific job functions as well as those that impact their broader role as a registrant employee. Compliance staff must design comprehensive training programs and consult on the development of department-specific training. Compliance staff must also stress the importance of training and enforce the timely completion of continuing education.

Supervision — Adequate supervision of employees as well as of outsourcing firms is crucial. Both the SEC and FINRA have published guidance on supervision generally as well as supervision of outsourced functions. Regulators expect supervisors to monitor and review subordinates' work and to escalate and document any noteworthy items or "red flags."

Auditing — An adequate audit requires more than simply testing whether a procedure was followed. It also entails testing employees' understanding of their responsibilities and how the compliance objective impacts their daily routines. Recommendations for improvement should be documented and plans to implement helpful recommendations should be developed and executed.

Conclusion

Maintaining, much less enhancing, compliance is costly and time-consuming. Although compliance may be seen as a nuisance by some — such as CEOs facing broader responsibilities in difficult economic times — ignoring it risks substantial harm, and potentially greater costs, to the business. As the SEC warns, now is not the time to neglect compliance practices.

Jeffrey F. Robertson is a partner in the Washington, DC office of Mayer Brown LLP. For nearly 15 years he has handled SEC enforcement and securities litigation matters and advised clients on securities compliance matters.

Akrivi Mazarakis is an associate in Mayer Brown LLP's Washington, DC office. A former attorney-advisor with the SEC's Office of Compliance Inspections and Examinations, she counsels broker-dealers, investment advisors and investment companies regarding compliance and related securities matters.

Related content

Related Articles

- 05 Jan 2009 - Broker-dealer compliance: 2008 in review
- 03 Dec 2008 - Making bricks without straw: compliance in the Age of the Budget Squeeze
- 21 Nov 2008 - How to manage compliance during a financial crisis
- 05 Nov 2008 - Building a strong culture of compliance through reward, not just preventing misconduct

News by Subject

- Compliance responsibilities and internal controls
- Risk

Directory

- Securities and Exchange Commission (USA)
- FINRA: Financial Industry Regulatory Authority

News by Country

- United States

Complinet | Connected Compliance ™

© 2009 Complinet Ltd and its contributors. All rights reserved.