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Better Management Through a Well-Defined Compliance Program

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Registered investment advisers (RIAs) overseen by the Securities and Exchange Commission (SEC) are required to comply with the Investment Advisers Act of 1940. Compliance, for many firms, can bring a cringe of fear or yawn of boredom and with busy schedules, it can be easy to put this important function on the back burner. However, when that dreaded audit letter or phone call from an SEC auditor arrives, firms often wish that compliance had been on the front burner all along. Thankfully, there exists a tool that, when used properly, can act as an open-note test for SEC audits and compliance. Enter a firm's policies and procedures, or as it is better known, the compliance manual.

Every firm needs policies and procedures as required by the SEC, and the compliance manual is the best practice for outlining these. Consequently, it is typically one of the first items SEC auditors will request during an examination. For firms that have properly reviewed and customized this document, this is a good thing. However, if the advisor is using a boilerplate format, it can be an easy source of bullet points to fill the corrections letter following the auditor's visit.

Each firm's compliance manual is bound to be unique to the firm's process, but this article looks at the SEC required sections that all RIAs should have, if applicable. Note, in some cases, the SEC has published guidance only on minimum standards and additional policies and procedures not discussed here may be required. Beyond satisfying

these requirements, the compliance manual can be used to encourage a culture of compliance for the firm. To that end, this article recommends a structure, as well as a few simple methods, that advisors can use to turn this document from a compliance-only tool to both a compliance and management tool that makes your firm both better prepared for SEC audits and clearly defines roles, responsibilities, and repercussions in a way that all firm employees can understand and willingly buy into.

SEC REQUIREMENTS FOR FIRMS' COMPLIANCE MANUALS

The need for policies and procedures originated out of Rule 206 (4)-7 of the Investment Advisers Act of 1940 and was adopted by the SEC on February 5, 2004. RIAs must¹:

- Develop written policies and procedures "reasonably designed" to prevent the adviser and its supervised persons from violating the Investment Advisers Act,
- Designate a chief compliance officer (CCO) and empower this individual to administer the policies and procedures, and
- Review and update these procedures on at least an annual basis.

Every advisor is apt to have unique policies and procedures because operational and compliance risks may differ from firm to firm. However, in a 2010 publication, the SEC "stated that it expects your policies and procedures, at a minimum, to address the following issues [ten areas], to the extent that they are relevant to your business."²

These 10 areas are the following:

1. Portfolio management processes: The allocation of investment opportunities among clients and consistency of portfolios with clients' investment objectives, disclosures by the advisor, and applicable regulatory restrictions
2. Trading practices: The procedures the RIA uses to satisfy its best-execution obligations, use of "soft dollars" to obtain research and services, and allocation of aggregated trades among clients
3. Supervised person: Trading of both the RIA and supervised persons
4. Disclosures: The accuracy of disclosures made to investors, clients, and regulators, including account statements and advertisements
5. Safeguarding of client assets: The safeguarding of client assets from conversion or inappropriate use by firm owners and staff
6. Required records: The accurate creation and maintenance of required records, which must be kept secure from unauthorized alteration or use and protected from untimely destruction
7. Marketing: A firm's marketing efforts, including the use of solicitors
8. Valuation: The valuation of client holdings and assessment of investment advisory fees based on those valuations
9. Privacy protection: A firm's policies and procedures governing the privacy and protection of client information
10. Business continuity plans: Developing and having in place a business continuity plan

The SEC gave us a starting point in the 10 commandments, but unfortunately it did not provide prewritten compliance manuals to all firms (see table 1). The sections below will outline a recommended structure that best incorporates the above requirements. The policies and procedures discussed are not an all-encompassing list, and additional policies and procedures may be required. Note: The appendix provides detail that expands upon the content of certain sections.

Table 1

CONNECTING THE COMPLIANCE MANUAL AND SEC REQUIREMENTS

Compliance Manual Section	SEC Requirement Discussed
Management Oversight and Sanctions	None
Code of Ethics and Personal Trading Policy	Supervised Persons
Record-Keeping Policy	Required Records
Privacy Policy, Cybersecurity	Privacy Protection
Trading and Brokerage Policy, Proxy Voting Policy	Trading Practices, Portfolio Management
Portfolio Management	Portfolio Management, Valuation
Custody and Possession of Client Assets	Safeguarding of Client Assets
Client Disclosures Policy	Disclosures, Portfolio Management
Communication Policy	Marketing, Disclosures
Outside the Manual	Business Continuity Plan

Management oversight and sanctions.

These sections are the introduction of the compliance manual. They do not specifically cover any of the SEC’s required policy areas, but beginning a firm’s manual in this way helps lay the groundwork for the sections that follow. Firms can state that they adhere to the three previously mentioned requirements of SEC Rule 206 (4)-7 and will review the compliance program annually. This is also a good place to identify the firm’s CCO and outline the roles and responsibilities of this individual. Also of importance is the policing of a firm’s policies and procedures, specifically how violations should be dealt with including whom a violation should be reported to (typically the CCO), and how sanctions should be levied on the violator.

Code of ethics and personal trading policy. This section is foundational for encouraging a culture of compliance, and firms should use it to outline a code of ethics. Advisors are encouraged to develop a strong code of ethics and firms may even desire to adopt the code of a professional body such as the CFA Institute or the Certified Financial Planner Board of Standards. If you do decide to adopt another body’s code, keep in mind that you must then follow those policies and procedures; don’t claim false adherence simply for appearances sake. Firms also should use this section to outline employee trading rules, including the firm’s insider trading policies, and reporting requirements for employee holdings and transactions

(including reporting exceptions). There are a few additional recommended sections related to employee disclosures and reporting requirements that firms can also consider including here. This section serves to satisfy the SEC’s requirement to develop policies and procedures surrounding trading of both the RIA and supervised persons.

Record-keeping policy. Action—or in this case, documentation—speaks louder than words. Inclusion of this section will address the SEC’s requirement to develop policies and procedures surrounding the accurate creation and maintenance of required records, which must be kept secure from unauthorized alteration or use and protected from untimely destruction. The general rule when it comes to documentation is that a firm’s records must be maintained for a minimum of two years on location at the firm’s home office, and three additional years in an easily accessible place, for a total of five years. Note that certain items may require different retention periods beyond the five years. As a recommendation, given the breadth of information a firm is required to keep records on, it may be helpful to specify all the requirements in an appendix to the firm’s compliance manual to avoid cluttering the main document.

Privacy policy. Hand in hand with the trust clients place in your firm to

manage their money is the discretion expected of your firm when it comes to managing their finances. The implication is that no client information is shared with outside parties unless otherwise guided by the client, or where the firm has previously disclosed to the client when it is required or permitted to share information. As part of this, firms are required to send out a privacy notice describing their policies and procedures surrounding client information, including any exceptions to client information sharing. This notice is sent annually, at the start to a new client relationship, upon amendment of the policy, or by client request and it should give the client the right to opt out of this information sharing. Firms should develop policies and procedures related to a firm’s technological and physical safeguards (i.e., firewalls, anti-virus software, shredding machines, locked storage of physical files, etc.), administrative safeguards (i.e., password reset frequencies, safeguarding of personal information in electronic communication, employee training, etc.), and third-party vendor policies as well as other methods used by the firm to uphold the privacy of its clients and their information. This section, in part, satisfies the SEC’s requirement to develop policies and procedures around privacy protection. This topic will be further covered when discussing cybersecurity below.

Trading and brokerage policy.

Conflicts of interest are easy to come by without well-developed policies and procedures relating to the trading of client assets. Firms should identify the custodian(s) used for custody and trading of client assets. Annually, firms are required to conduct a “best-execution” review, and as part of this, they must evaluate their current custodian relative to alternatives. A firm should discuss the criteria it looks for when selecting a custodian and how the firm’s current custodian satisfies these criteria. When designing policies and procedures surrounding trade aggregation and allocation of investment opportunities, it boils down to the equitable treatment of all clients. Other policies and procedures that fall under this heading include a firm’s policies on trade errors, client-directed brokerage, soft-dollar practices, and proxy voting. This section of your compliance manual covers the SEC’s policy requirement around trading practices such as procedures the RIA uses to satisfy its best-execution obligations, use of “soft dollars” to obtain research and services, and allocation of aggregated trades among clients. It also partially satisfies the required policies of portfolio management, specifically, allocation of investment opportunities among clients.

Portfolio management. A few of the SEC’s required policies are covered in this part of the manual, such as a firm’s portfolio management processes, including consistency of portfolios with client’s investment objectives and applicable regulatory restrictions, as well as the valuation of client holdings and assessment of fees. This section encompasses how a firm assesses its advisory fees and how it manages client assets. The firm should outline its process for valuing the assets it manages and how it values client assets where a custodial price or value is not readily attainable. As part of this, a firm’s billing practices and how advisory fees are assessed must be explained. The second part of this section lays out the firm’s management of client

assets, namely the model portfolios and strategies used by the advisor, and the process for determining and reviewing which strategies best fit a client.

Custody and possession of client

assets. Custody of advisory client assets is defined as having direct or indirect access to such assets. The firm should outline potential custody risk areas to be disclosed to the CCO. From this, a firm should outline policies and procedures that help employees avoid triggering a custody situation or navigate such a situation if they find themselves in it. A firm should discuss whether it has triggered the custody rule and if so, discuss its associated third-party audit requirements. If a firm has determined it has custody of client assets, it is required to enter into a written agreement with an independent public accountant registered with the Public Company Accounting Oversight Board to conduct an annual surprise inspection of the firm. Lastly, firms can use this section to discuss policies and procedures related to money movement, particularly those involving third parties. This section serves to satisfy the SEC’s requirement for policies surrounding the safeguarding of client assets from conversion or inappropriate use by firm owners and staff.

Client disclosures policy. Discussion of a firm’s Form ADV Part 2 and Privacy Notice is covered in this section. Firms should detail both the delivery and filing requirements for both documents. The information in this section and its associated documents covers the disclosures by the advisor requirement of the SEC’s policies and procedures on portfolio management processes and the policies and procedures surrounding the accuracy of disclosures made to investors, clients, and regulators.

Communication policy. This section serves to satisfy the SEC’s required policies on the firm’s marketing efforts, including the use of solicitors, and further outlines policies and procedures

around the accuracy of disclosures made to investors, clients, and regulators, including account statements and advertisements. It is designed to guide the firm in avoiding misleading statements to current and potential clients. Care should be taken when communicating information in written, verbal, or digital form, particularly performance-related information, to outside parties. A firm should develop specific policies and procedures governing its advertising and marketing efforts and detail how clients receive information about their accounts (i.e., custodial statements, independent performance report mailings, etc.). Lastly, if a firm utilizes solicitors, the nature of this relationship, including compensation, can be outlined here.

Other sections. Policies and procedures change over time and the SEC, since issuing minimum requirements for advisors’ policies and procedures in 2010, continues to develop new guidance for advisors. Most recently, the SEC has emphasized that firms should develop policies and procedures for cybersecurity and aging clients. When it comes to the former, a discussion of a firm’s data storage and back-up policies, network security, password protection, and safekeeping of firm hardware must be outlined. This section serves to satisfy, in part, the SEC’s requirement to develop policies and procedures around privacy protection along with the previously discussed Privacy Policy section of the manual. The section on aging clients is aimed at mitigating elder abuse and monitoring for signs of diminished capacity. A “senior client” in the SEC’s eyes is anyone older than age 62, a client who is retired, or a client transitioning to retirement. Firms and their employees are required to be exceedingly vigilant when meeting with clients who meet these criteria and should invite these clients to specify a trusted individual (non-spouse is recommended) to contact if the advisor suspect signs of elder abuse or diminished capacity.

Business continuity plan. Not all SEC requirements should be packed into a firm's compliance manual. As a suggestion, the business continuity plan can function best as a stand-alone document that employees can reference quickly and easily. At a very basic level, this document should cover: (1) A disaster recovery location should the firm experience a disruption that prevents effective operations from its current office environment (2) identification of the disaster recovery team, (3) designation of the duties each member of the team is responsible for to get the firm back up and running, (4) employee and critical service provider contact sheet, (5) outline of backup and recovery procedures for electronically stored information, and (6) a commitment to update and review the document with firm employees annually. The compliance manual must be tailored to the way your firm operates. There is no one-size-fits-all manual, and often boilerplate policies and procedures do more harm than good.³

A streamlined manual with meaningful policies and procedures is preferred to one filled with procedures that do not apply to the RIA's business model.

TAKING YOUR MANUAL FROM A COMPLIANCE TOOL TO A MANAGEMENT TOOL

After incorporating the required SEC sections, customizing the compliance manual to suit your firm's operations, and reviewing it annually, it may feel that the work is done. But would it not be more beneficial if, after all the time you spent on this document, it could be used as a management tool as well as a compliance tool?

Firms often start with a boilerplate document at inception, then over time fully rewrite and customize the policies and procedures. To the extent that firms create a document that employees and managers can easily understand, practically use, and buy into, it would be beneficial for the firm to do so. The following suggestions are tweaks that can encourage a culture of compliance.

COMMITTEE REVIEW

When writing new policies and procedures, or evaluating current ones, use a committee structure. Having the CCO solicit input from management such as managing partners, chief operating officers, or directors is the first step to going from a compliance-only tool to a management tool. Additionally, it further promotes buy-in from senior leaders of the firm.

Consider creating a binder for firm employees containing documents such as the employee handbook, compliance manual, and other day-to-day information employees may need to reference.

VISIBILITY

The less this document gathers dust on the shelf, the better. Consider creating a binder for firm employees containing documents such as the employee handbook, compliance manual, and other day-to-day information employees may need to reference (e.g., the firm's approved investment list for trading). This binder should be easily accessible to senior managers and sit at each employee's desk, or if there is a firm intranet, it could be in an easily accessed electronic location. Grouping the compliance manual with other frequently referenced documents can make it a familiar resource for senior management and employees. A document that is visible and promoted emphasizes its importance to the firm.

FORMATTING

Good management goes hand in hand with accessibility and transparency. As such, your compliance manual should be simple and well-formatted. Employees should be able to access the document for reference at any time (either in paper

or digital format). To make their navigation of the document as easy as possible consider the use of a table of contents, with clickable document links (for the digital copy) in each section as a small but beneficial navigation tool. Likewise, when referencing another section of the manual, it is helpful to include an intra-document link so the reader can jump quickly between the current section and the referenced section and vice versa.

ANNUAL DISCLOSURES

Employers are required to pass out and collect signed copies of the code of ethics and personal trading policy each year, but why not the entire compliance manual? To streamline things, combine the process for reading and acknowledging the manual with the disclosures an employee is required to make (i.e., holdings, transactions, etc.). The review of the compliance manual then becomes a more substantial compliance packet composed of: compliance manual, code of ethics, personal trading policy, business continuity plan, fourth-quarter personal transactions, annual holdings, gifts given or received, outside business interests, outside positions (directorships, board memberships, trusteeships, power of attorney, etc.), trade errors, and political donations.

These items also are recorded during the year. For example, trade errors should be disclosed to the CCO immediately upon discovery; however, this serves as a catch-all disclosure process and makes it about more than simply reading the manual.

EMPLOYEE BUY-IN

On the front cover of this annual packet should be a signature page with an attestation such as the one below:

Employee Attestation

I certify that by signing below and by my initialing where provided at the beginning of each section within the manual, that I have received a copy of and read the Compliance Manual,

Code of Ethics, and Business Continuity Plan / Disaster Recovery Plan in their entirety and understand the guidelines I am to follow and the responsibilities I am charged with.

I recognize that failure to follow the guidelines and responsibilities laid out in this manual is a violation of the Employee Code of Conduct and may result in disciplinary action.

The directness of this statement encourages employees that it would be in their best interest not to merely skim. For a further incentive to read through the manual, require employees to acknowledge that they have read each section. Employees must initial at the beginning of each section to indicate they have read and understood that particular section. Both are designed to get the employee to have more skin in the game when it comes to reviewing and understanding the firm's policies and procedures.

QUESTIONNAIRES

To ensure employees are not merely dotting the I's and crossing the T's, require each employee to complete an annual test. Nothing overly taxing, but a questionnaire with 5-10 different questions each year can be helpful. Specifically, it can be used to shed light and understanding on new policies and procedures recently added to the manual and test areas the CCO has noticed the firm has been lax in its understanding of. Firms also may find that smaller but more frequent quarterly quizzes work better to increase the visibility of this document.

ACTIONS AND FOLLOW-UPS AS MANAGEMENT TOOLS

Compliance manuals tend to be long-winded, even when customized to the firm at hand. After reading through a section, it may be hard to keep track of what needs to be done and who is responsible for doing it. The concept of an action and follow-up summary section to conclude each part of the manual can help.

The action has the purpose of summarizing the important steps a firm must take as detailed in that section of the manual. For example, in the client disclosures policy section of the manual, we use the following:

Action: *[Firm Name] will provide new clients with a copy of Part 2 of Form ADV at the time of entering into the contract. Additionally, [Firm Name] will provide all clients with a copy of Part 2 of Form ADV on an annual basis (and make a note of the date of mailings) or a copy of the brochure upon written request (within seven days of request receipt).*

This section serves to boil down each section of the manual to the key points on which a firm is required to act.

The follow-up serves as management's tool for confirming that what is outlined in the action section is being completed and designates an individual to verify completion. In this section of the compliance manual, it reads:

Follow-up: *The CCO will keep a copy of all documents sent to clients, as well as a list of who was sent a copy of the document and the date of the mailing.*

This section identifies that the CCO is responsible for confirming the outlined action items were completed by keeping documentation of the annual ADV mailings, and who was sent this document, as well as when.

The action and follow-up format can be after each section of the manual, or if it is a longer and more complex section, it may be beneficial to include actions and follow-ups after important subsections. These actions and follow-ups then become a short-form operating manual for employees and management and provide an actional path, concisely outlining both what must be done and who

is responsible for accomplishing this requirement.

All material within a firm's compliance manual can be tested by auditors during their review. If there is concern about the potential accountability of using the action and follow-up structure within the main body of the compliance manual, consider splitting the manual into two separate documents—the compliance manual and an accompanying guide, which separately details these action and follow-up items. Firm employees can view these two documents as one when referencing the firm's policies and procedures.

CONCLUSION

A firm's compliance manual can serve as more than a dusty requirement. A few easy edits can turn this document from a compliance-only tool to a management tool.

Although the SEC has published minimum requirements for policies and procedures, new guidance is always coming out and it is an ever-changing environment, as the recent emphasis on cybersecurity and aging clients shows. Firms' policies and procedures can and will be tested beyond these minimum requirements. This article is a starting point; firms are advised to partner with a subject matter expert such as a compliance attorney to develop comprehensive compliance programs. To further stay up to date with compliance focus areas, consult the SEC website, where it publishes "Examination Priorities" for each year. These can serve as a quick check for existing policies and procedures and help firms stay abreast of new developments.

As a final reminder, "Not all compliance failures result in fraud, but many frauds take root in compliance deficiencies."⁷⁴ ●

APPENDIX

Note: Additional items may be required to comply fully with SEC rules and regulations. It may be advisable to partner with a subject matter expert such as a compliance attorney.

CODE OF ETHICS AND PERSONAL TRADING POLICY

To be effective, RIAs must adopt a code of ethics⁵ that:

- At a minimum, will require employees to comply with federal securities law, and emphasizes a firm's fiduciary obligation.
- Outlines the reporting requirements for employees' personal securities transactions and holdings when first starting at a firm and after that; additionally, the advisor should designate an individual (e.g., the CCO) to identify improper trades or trading behavior and report such violations.
- Discuss how employees are required to obtain approval before investing in initial public offerings (IPOs) and private placements.
- Lastly, all RIAs are required to provide a copy of the code of ethics to all firm employees and to receive back written acknowledgment of receipt.

Employee trading of personal assets should be in line with the firm's code of ethics:

- An employee should consider the impact of personal trading (including non-paying accounts of household family members, and those over which the employee has authority) on the firm's clients and whether it will disadvantage any of the firm's client base.
- Firms should have in place a well-developed insider trading policy.
 - › Any individuals associated with the firm are prohibited from engaging in any securities transaction for their benefit or the benefit of others while in possession of insider information.

- › A firm should lay out a plan of action for the CCO when insider information is brought to its attention, including potential sanctions.

Employees are required to report (for both themselves, as well as other accounts they have direct and indirect influence over):

- Holdings should be reported annually, and no later than 45 days past the date the report was submitted. For new employees, holdings must be reported within 10 days of hire and should be current within 45 days of the date the report was submitted. The report should include:
 - › Security name, identifier (ticker, CUSIP, etc.), number of shares, principal value
 - › Institution the investments are held with and account number
 - › Date report was submitted
- Transactions should be reported quarterly, and no later than 30 days past quarter-end. The report should include:
 - › Date of transaction, security name, identifier (ticker, CUSIP, etc.), interest rate and maturity date, number of shares, principal value, the price at which transaction occurred
 - › Nature of transaction (buy, sell, etc.)
 - › Institution the investments are held at and account number
 - › Date report was submitted

This section also should define the exceptions to these reporting requirements and what constitutes a reportable investment holding. The CCO is responsible for reviewing the above reports and should have employees' holdings and transactional reports reviewed by a senior member of the firm.

There are a few additional policies and procedures that one can outline in this section of the manual related to employee disclosures:

- Acceptance and giving of gifts over "de minimus" value
- Service as director/board member/power of attorney/trustee
- Outside business interests

Any violations to the firm's code of ethics or personal trading policy should be reported promptly to the firm's CCO, and the decision to levy sanctions on the violator may be considered.

RECORD-KEEPING POLICY

A firm should maintain copies of the following:

- Code of ethics, personal trading policy, and compliance manual. (Note: Code of ethics copies should be kept for five years from the date they were last in effect.)
- ADVs, including to whom the Form ADV Part 2 was delivered, the date it was delivered, and its method of delivery; any requests for a copy of the firm brochure should be noted as well.
- Records of any violations of the compliance manual, as well as if any corrective action was taken as a result.
- Signed copies of the code of ethics, personal trading policy, and compliance manual from each firm employee. (Note: Signed employee acknowledgments should be kept for five years after the employee ceases to be a supervised person.)
- An organizational chart detailing a list of names of current employees and access persons.
- A list of employees terminated over the previous five years.
- Holdings and transactions reports of employees.
- Records of decisions approving security acquisitions (including IPOs and private placements) along with the documentation of why they were approved.
- Financial records of the firm (financial statements, bank statements, bills, etc.)
- Client records (statements, communication, etc.).

- Investment records (transaction confirmations, trade proposals, confirmations, proxy voting, etc.).
- Performance data used in marketing documents. (Note: This information is required to be maintained for five years following the end of the fiscal year in which the document was last used for marketing purposes.)
- Other administrative and compliance records including corporate documents, which need to be maintained at the office for the life of the business and in an easily accessible place for three years following the notification of business termination to the SEC.

Additional information on these record-keeping requirements can found at the below-referenced sources.⁶

PRIVACY POLICY

A firm should detail the situations in which it is required or permitted to share end-client information, namely:

- To complete transactions or account changes as directed by the client (talking with the client's attorney, CPA, etc.)
- To maintain or service a client's account
- If requested to do so by a client
- With contracted providers providing administrative functions for the firm (i.e., third-party reporting software, custodian, the firm's attorneys/accountants/auditors, etc.)
- If the firm is required or permitted by law or regulatory authorities with regulatory jurisdiction over the firm

TRADING AND BROKERAGE POLICY

Additional detail on a firm's trade error policy:

- A firm should outline what does and does not constitute a trade error and what is the process to rectify an error once discovered.
- It is required that a firm will always make the client whole in the event a trade error results in a loss.

- In the event of a gain, RIAs have more say in how this is treated. It may be helpful to have a separate appendix to formally define what does and does not constitute a trade error to avoid cluttering the main document.

PORTFOLIO MANAGEMENT

Additional detail on a firm's advisory fee policy that should be outlined in the policies and procedures:

- Are clients billed in advance of the quarter or in arrears?
- Does the advisor adjust for additions and withdrawals during the quarter? Keep in mind that if billing in advance, advisors are required to refund in a pro-rata manner clients that terminate their advisory relationship during the quarter.
- How are the fees calculated, and what is the process for verifying these calculations and preventing errors?

Additional detail on model portfolios and model strategies used by the advisor:

- How many models are offered and what is their range of risk (i.e., conservative to aggressive)
- The initial process for determining which investment model is best for the client during the initial stages of a relationship
- How often is a client's model portfolio reviewed during the relationship and assessed for appropriateness
- How often are client portfolios reviewed, and what triggers a rebalance of a client's portfolio

CUSTODY AND POSSESSION OF CLIENT ASSETS

To avoid inadvertently triggering custody of client assets (beyond having the ability to deduct advisory fees from client accounts), it is advised that without CCO authorization, firm employees should not:

- Serve as a trustee or power of attorney over client accounts

- Have check-writing authority for client accounts or bill-paying authority
- Manage client accounts outside of their custodian through use of personal logins and passwords that may grant authority to withdraw funds and transfer assets from client accounts
- Receive checks made out to advisory clients and fail to return promptly
- Take physical possession of client security certificates
- Serve as general partner of a limited partnership

CLIENT DISCLOSURES POLICY

Regarding the firm's Form ADV Part 2 and privacy notice:

- Firms are required to provide these to clients before or at the time an advisory agreement is entered.
- The firm's annual amendment update must be filed within 90 days of its fiscal year-end and delivered to advisory clients within 120 days of fiscal year-end (typically the privacy notice is provided in conjunction with this mailing).
- As part of this annual delivery, a firm is required to denote any material changes and offer to provide the complete firm brochure (including advisor-specific brochures) should a client request it.
- Firms are required to send a notice to clients anytime a material change occurs to the business that could impact the advisory relationship versus waiting until the annual filing.

COMMUNICATION POLICY

In general:

- All client communication should strive to be presented fairly and disclose all material facts the audience may find beneficial to the decision-making process.
- Where appropriate, disclosures should be used as dictated by the CCO, and the CCO should be consulted for the final review of communication items.

- Should a written complaint arise, employees should forward it to the CCO for review and archiving.
- If performance data is shown, it is recommended it be presented net of advisory fees, brokerage commissions, and other expenses.
- Advisors are prohibited from using client testimonials in marketing materials.
- If performance is something the firm wants to include in advertisements, it needs to disclose all recommendations within at least the prior year. As part of this a firm should disclose: security recommended, date and trade (i.e., buy, sell, etc.), market price of trade, reasonable current market price of security, and a disclosure that “it should not be assumed that recommendations made in the future will be profitable or will equal the performance of the securities in this list.”
- Advertisements or marketing materials must not include false, untrue, or otherwise misleading statements. Additionally, any discussion of investment strategies needs to provide a basic overview of the strategy, including its potential limitations and risks to give the end-user full and clear information.
- The reference of designations by the firm’s investment professionals or awards received by the firm itself should not be exaggerated or over-promise the firm or individuals’ capabilities as a result of this award or designation.

OTHER RECOMMENDED/ REQUIRED SECTIONS

When establishing policies and procedures in the cybersecurity section of the manual, firms should:

- Outline policies surrounding where data is stored and backed up. The firm should be knowledgeable on the network security systems in place such as firewalls, malware protection, etc.
- Maintain an inventory of all hardware capable of storing sensitive information (laptops, external hard drives, etc.).
- Outline password policies (i.e., the strength of passwords, frequency of reset, not allowing auto-login options for hardware or client information sensitive websites, what the firm does with shared logins in the event an employee leaves the firm, etc.).
- General policies for the workspace (i.e., computers should not be left idling and should be shut down at the end of the day, clean desk policy, keep physical client documents locked, etc.).
- Additionally, in the event that sensitive hardware is lost, or there is a suspicious activity surrounding a client, such events should be reported to the CCO for the determination of next steps and to be logged.

For policies surrounding aging clients:

- It is recommended that firms and their employees undergo training to

better identify both signs of diminished capacity and elder abuse.

- Firms are required to review annually the suitability of portfolio targets of senior clients that are more aggressive than a firm’s more conservative models. Note: What is considered a conservative model has some firm interpretation available to it.
- Firms should encourage their senior clients to complete a trusted contact form that gives the advisor and client a trusted third party to whom the advisor can communicate and confirm signs of diminished mental capacity or elder abuse to determine next steps (i.e., the establishment of power of attorney).
- Any signs of diminished capacity or elder abuse should be documented. Any issues related to elder abuse should be escalated to the CCO who should contact the proper authority.

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ENDNOTES

1. See <https://www.sec.gov/rules/final/ia-2204.htm>.
2. See <https://www.sec.gov/divisions/investment/advoverview.htm>.
3. Les Abromovitz, *The Investment Advisor’s Compliance Guide* (National Underwriter Company, 2012).
4. Robert Khuzami, former director of the SEC’s Division of Enforcement.
5. See endnote 3.
6. See <https://www.sec.gov/divisions/investment/advoverview.htm> and endnote 3.



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