



IAA INVESTMENT ADVISER
COMPLIANCE
CONFERENCE 2022

MARCH 3-4, 2022 / JW MARRIOTT / WASHINGTON DC
EFFECTIVE STRATEGIES & BEST PRACTICES

Back to Basics Track

Annual Reviews

Evolutions and Implementation Strategies

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EFFECTIVE STRATEGIES
& BEST PRACTICES

How Robust Does Your Compliance Program Have to Be?

- Lessons learned from enforcement actions
- Recent *Risk Alerts* provide guidance
- Common SEC exam themes
 - Competence of the CCO
 - Compliance Program must be effective
 - Inadequate Resources
- **Discussion:** Top resources to turn to conduct the Annual Review
 - See “Questions Advisers Should Ask When Establishing or Reviewing Their Compliance Programs” (May 2006)

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How Robust Does Your Compliance Program Have to Be?

Practical Tips

- Use regulatory risk/conflict matrices to identify potential “gaps” or action items
- Develop a practical Compliance Manual
 - Consider having separate Operations and Supervision Manuals
- Monitor, test and report on procedures
 - Consider independent compliance program testing and mock regulatory exams

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How Robust Does Your Compliance Program Have to Be?

Annual Review Plan

- As part of the Annual Review process, also develop and/or ensure the firm has:
 - Remediation plans
 - Training programs
 - Senior management involvement
- Prevent problems with effective supervision
 - Consider if managers understand their oversight responsibilities and escalation processes

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The Annual Review is an Ongoing Process

Focus on Risk-Based Approach

- The SEC asks advisers to evidence evaluation of high-risk areas
- How to begin the assessment:
 - Identify and evaluate potential conflicts of interest and consider sufficient checks and balances to address them
 - Review past SEC deficiency letters
 - Review past compliance discrepancies
 - Identify new lines of business or products
 - Consider SEC priorities and recent *Risk Alerts*

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The Annual Review is an Ongoing Process

Type of Testing and Frequency

- Step 1: Evaluate **transactional tests** to help identify high risk areas
- Step 2: Establish **periodic testing** at appropriate intervals to verify compliance with relevant requirements
- Step 3: Conduct forensic testing to critically test an activity to determine whether the compliance system is being circumvented
- **Discussion:** What is the frequency of your annual review? How is it conducted?
 - See Gene Gohlke, speech “Practical Guidance for Hedge Fund CCOs Under the SEC’s New Regulatory Framework” (May 2005)

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The Annual Review is an Ongoing Process

Documenting the Annual Review Results

- The Report should be in writing and memorialize:
 - Identified risks and how they are managed and mitigated
 - The types of tests performed, when, and results/findings
 - Actions, if any, to be taken to address risk areas
- Supporting documentation (such as exception reports) often is requested during SEC exams; this helps to support findings
- **Discussion:** What methodology is used to conduct testing (e.g., interviews, reconciliation, etc.) and how is this documented
 - See Sample Compliance Review Sheets

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How Much Is Enough for the Annual Review?

Deploy Effective Procedures for Testing

- A systematic approach requires that you are consistent
 - Identify who is responsible and what duties are to be performed
 - Determine testing frequency and where findings are evidenced
 - Assess which business units are performing other tests as part of his/her role and gather those results
- Technology can be a significant component to testing
- **Discussion:** Which business areas perform daily activities, periodic or forensic testing that you find helpful for the Annual Review?
 - See Lori A. Richards, speech “Put the Compliance Rule to Work” (March 2004)

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How Much Is Enough for the Annual Review?

Consider Guidance from Recent *Risk Alerts*

OCIE Observations: Investment Adviser Compliance Programs (Nov. 19, 2020)

- Inadequate Compliance Resources
 - Advisers did not devote adequate resources, such as information technology, staff and training, to their compliance programs
- Insufficient Authority of CCOs
- Annual Review Deficiencies
 - Lack of evidence of Annual Review, identification of risks, and review of significant aspects of adviser's business
 - Advisers did not devote adequate resources, such as information technology, staff and training, to their compliance programs

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Identifying and Documenting Issues

Client Facing Summaries vs. In-House Annual Report

- CCOs have a duty to inform their senior management team details relating to their findings
 - This information may trigger changes in the organization
- Client facing summaries generally provide a big-picture view of the compliance program
 - Typically used as part of a due diligence process
- **Discussion:** Do you prepare two forms of Annual Review reports?

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Identifying and Documenting Issues

What To Do With What You Discover

- If a risk is identified and there are no policies or procedures, develop and adopt new policies and procedures
- If there is a material problem, discuss with outside counsel
 - Consider if clients need to be made whole and/or if new internal controls should be developed
 - Evaluate if a policy needs to be changed and/or if training needs to occur

Discussion: What is the biggest challenge you have faced when identifying a problem? How did you handle that situation?

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Final Thoughts

- Be proactive, not reactive
- Use data analytics to manage and identify risks
- Follow through on new risks identified
 - Consider how the firm is addressing the risk
 - Review your policies and procedures routinely and revise as needed
 - Stay apprised of new *Risk Alerts*
 - Maintain strong and frequent communications with senior management, employees and clients which will help to identify gaps and advance compliance efforts

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Supplemental Materials

- Core Compliance Risk Management Update - *Considerations for Advancing Your Compliance Program*
- IA Compliance Program Essentials (Supplemental Presentation Outline)
- IAA - *Compliance Control: Interim Annual Compliance Program Reviews*
- Jacko Law Group - *Top 10 List for IA Annual Reviews*
- Jacko Law Group - *What the SEC Really Wants to Find in Your Firms Compliance Manual*
- Sample Compliance Review Sheets
- SEC - Questions Advisers Should Ask While Establishing or Reviewing Their Compliance Programs (May 2006)
- SEC Risk Alert – *OCIE Observations: Investment Adviser Compliance Programs* (Nov. 19, 2020)
- SEC Speech (Gene Gohlke) – *Practical Guidance for Hedge Fund CCOs Under the SEC's New Regulatory Framework* (May 5, 2005)
- SEC Speech (Lori A. Richards) – *Put the Compliance Rule to Work* (March 15, 2004)

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Q&A - Let us know how we can help!



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The banner features a teal background on the right and a blurred image of colorful light trails on the left. The text is white and includes the conference title, dates, location, and a subtitle.

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