

NSCP CURRENTS

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Investment Adviser Compliance Training

By Lorna A. Schnase

Although broker-dealers have been subject to detailed training requirements for over a decade,¹ investment advisers are still coming to grips with training under the relatively recent Advisers Act compliance rule,² which requires advisers to adopt a compliance program reasonably designed to prevent violations but leaves it to each adviser to determine what training is appropriate for them to achieve that end. This article discusses a number of ideas advisers might use to build an effective and efficient training plan as part of their compliance program.

We're All in This Together

Too often an adviser's Chief Compliance Officer ("CCO") becomes the sole focus of an adviser's compliance training effort because, fairly or not, the CCO bears a disproportionate share of the adviser's compliance burden, being expected to be "competent and knowledgeable" about the Investment Advisers Act of 1940 ("Advisers Act")³ and having the explicit responsibility to administer the adviser's compliance program.⁴ However, compliance training is equally important for the adviser's other personnel because CCOs don't "do" compliance.⁵ Rather, each and every person in the firm must "do" compliance in their areas of

activity, as part of an overall program which is administered by the CCO. Advisers can be held vicariously liable for compliance failures committed or caused by their employees in the course of their employment.⁶ Moreover, employees can be held *personally* liable for their own violations, in addition to creating liability for their firm.⁷ In that sense, then, advisers and their personnel truly are in this together.

We all know that ignorance of the law is no excuse. Increasingly, ignorance of the firm's internal policies and procedures and ignorance of the SEC's expectations are no longer an excuse either. Consequently, it is essential that personnel be trained to the extent necessary for them to stay in compliance with *all* applicable laws, procedures and other requirements and, in that way, keep the firm in compliance as well. Training should be available not only to employees who may seem to pose less risk to the firm's compliance (receptionists, mailroom personnel, clerical assistants, etc.), but to all personnel, including the most senior executives, whose enthusiastic involvement in compliance training will help to set the "tone at the top" and promote a "culture of compliance."

Although it is important for everyone to be included, it is not the case that "one size fits all" when it comes to appropriate compliance training. Certainly, there is a need to train everyone on basic requirements and on-going developments with firm-

wide significance, but the most effective training plans also include a component focused on individual employees, tailored to their background, needs and areas of responsibility. This makes training more interesting and relevant and fosters an environment conducive for employees to "buy into" the training program. Importantly, it also avoids a waste of time and money.

For those reasons, wise advisers will devise and implement a compliance training plan along a dual track, one track addressing the overall needs of the firm and another plotting out for each employee whatever training is appropriate for them.⁸

Turn Everyday Items into Training Tools

There is a widespread misunderstanding that effective training has to be time-consuming and expensive. Not so. Following is a discussion of tools that advisers might use when devising and implementing their training plans. Many of these tools are already being used at advisory firms for other purposes and can simply be broadened or co-opted to serve a training function as well.

It is of course not necessary that all these items be used in every adviser's training plan, but they should be considered and pursued to the extent an adviser finds them useful. Some of these tools will be more suited to use at the firm level. Others will be more suited to use at the employee level where more individualized attention is appropriate.

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Internal Resources

New employee orientation.

Historically, new employee orientation has been largely an HR function, concentrating on insurance forms, access keys and computer systems. However, allowing a new employee – no matter how senior or experienced – to begin work at an advisory firm without a thorough understanding of the firm’s compliance policies and procedures is a violation waiting to happen. Employees should not only be provided a copy of the compliance manual and asked to sign an acknowledgment of receipt. Rather, someone knowledgeable about the employee’s area of responsibility should walk them through key compliance procedures affecting their area, stressing the importance of those procedures and addressing any questions. This process should also aim to uncover any differences in the firm’s procedures from those the employee may have been subject to at a prior place of employment.

Compliance manual and amendments.

Distributing the compliance manual to employees – and periodic amendments to it – is a prime opportunity to educate and train on compliance. The best compliance manuals are not just a litany of rules, forms and procedures, but include explanations of the policies and goals the procedures are designed to achieve. Periodic updates of the manual should be distributed to all personnel along with a memo or other mechanism for drawing attention to significant changes. Many advisers post their compliance manual on the firm’s intranet, so the most up-to-date version is instantly accessible both firm-wide and remotely. Amendments are distributed electronically along with a request for employees to specifically acknowledge that they received and read the amended items. Some CCOs spot check whether individuals in the firm actually received the amendment and engage them in a discussion to assess whether they really understood what it meant.

Annual in-house compliance training meeting.

While an annual compliance meeting has been common at broker-

dealer firms for many years, it is just now becoming common at advisory firms subject to the Advisers Act compliance rule. Some firms add the compliance meeting onto other annual firm functions, such as firm retreats or firm planning and budgeting meetings. The agenda usually recaps significant compliance items from the last year, along with a discussion of the hot compliance topics facing the firm in the coming year. Firm-wide meetings may be suitable for smaller firms with a limited agenda. Larger firms may find departmental or small group meetings more effective. In any case, it would be wise to ask participating personnel to sign an attendance sheet, to be kept along with the agenda of topics covered as part of the firm’s records evidencing implementation of the training plan.

One-on-one or small group training with experienced personnel.

In addition to an annual compliance meeting, CCOs or other knowledgeable personnel can meet with individuals or groups during the year to cover compliance topics of interest. Topics might be rotated to cover the “topic of the month,” selected based on recent problems encountered at the firm or recent SEC pronouncements, industry developments or similar catalysts. Making these sessions fun for employees encourages participation and helps to ensure that the information will be memorable. For example, one adviser uses a “quiz show” format for its compliance meetings, complete with candy bar prizes.⁹ Others interact with participants using a “what would you do if” interview technique, so participants are engaged and encouraged to think through issues in real-life situations. This also helps the CCO to identify where understanding is incomplete so that appropriate follow-up can be pursued.

Internal firm newsletters.

Firms often circulate newsletters to their personnel to keep them up-to-date on firm happenings and convey important internal information. Newsletters can serve an effective compliance training function as well, if relevant compliance articles or reminders are incorporated when and where appropriate.

Debriefings following a compliance “event.”

Often, the best time to learn from a painful experience is shortly after it happens, when memories are still fresh but the heat of the moment has given way to more considered reflection. For that reason, advisers should follow up on painful compliance events – violations, glitches, close-calls, SEC deficiency letters, client complaints and the like – by debriefing those involved soon after the event is over, with the aim of uncovering what happened and why, and how it can be avoided in the future. Too often the “crush of business” means that these learning opportunities slip away without a clear post-mortem analysis and understanding. In those cases, not only is a valuable object lesson lost, but a valuable training opportunity may be lost as well.

Performance reviews.

Any compliance problems in which an employee was involved should be part of the employee’s periodic performance review. Often the employee’s culpability in the problem is given consideration when setting the employee’s bonus or raise. As importantly, performance reviews can serve as an opportunity to identify and plan for an employee’s future training, including on compliance matters. Employees should be encouraged to identify any compliance areas where they feel weak and to suggest any training activities they know of that might address that weakness.

External Resources

CCOutreach seminars.

Each year, the SEC conducts national and regional CCOutreach seminars to address topics of interest in adviser and fund compliance. Although most firms find it appropriate to send only the CCO or other compliance personnel to these seminars, an audio webcast of the national seminar is archived on the SEC’s website for listening after the fact by anyone in the firm.¹⁰ Selected topics from the webcast can be incorporated into an adviser’s training plan where appropriate, without having to incorporate the entire seminar. Selected written materials handed out at the SEC’s regional CCOutreach

seminars can be utilized where useful as well.

Industry conferences.

There are a host of organizations that offer industry-related conferences, seminars and workshops aimed at training in adviser-related compliance, among them the NSCP, the Investment Company Institute and the Investment Adviser Association. Many of these conferences are now offered as webcasts, audio-casts, conference call-ins or similar means which allow more participants to have access to the information without incurring the time and cost of travel. This makes them increasingly valuable as training tools in firms where growing needs increasingly clash with tightening budgets.

Compliance certification programs.

A number of organizations¹¹ are now creating or offering adviser-specific compliance professional certifications or designations for those who register for and successfully complete a series of requirements. Although it is too soon to tell whether acceptance of these certifications will be widespread in the industry, the programs are aimed at training in key adviser and fund compliance areas and typically require candidates to maintain their certifications with continuing education. Although these programs are likely to be utilized primarily, if not exclusively, by CCOs and other compliance department personnel, relevant portions of the resources they make available could be used selectively as part of a firm's own training plan.

Training from outside vendors and service providers.

This is probably one of the most overlooked resources available to advisers for compliance training. Compliance training tailored to a firm's specific needs is available from many compliance consulting firms and commercial vendors who specialize in providing training and other compliance resources to advisers and their personnel. In addition, training is often available from an adviser's existing vendors and service providers, such as software vendors, law firms, accounting firms, custodians and the like. Many of these training opportunities can

be made available at no charge if the adviser would simply ask, particularly if the adviser is willing to have a presentation covering the general topic combined with a sales presentation about the provider's specific product or service available to address that topic. Other training tools are available on a "canned" basis (covering a topic of interest but not tailored to a particular adviser), often on-line and often at no charge. Even advisers concerned about the cost of consulting firms and commercial vendors should think broadly and inquire into what training resources might be available from their existing outside vendors and providers.¹²

Publications.

Now more than ever, publications addressing relevant compliance topics are available from an abundance of sources, including law firms, industry associations, print and on-line publishers, industry-related listservs, blogs and the like. As with the other resources already referenced, many of these are available at no charge. A well-crafted Internet search will uncover many of these resources, which can be used as tools to keep current on industry developments or as resources for researching specific issues.

Informal local compliance discussion groups.

In various cities around the country, compliance-related personnel from local advisory firms get together informally from time to time to discuss developments and topics of interest in the industry. City-specific meetings offer a local flavor that may not be available at national or regional conferences and allow for a more informal sharing of experiences and knowledge without the time, cost and inconvenience of travel. Although compliance department personnel make up the bulk of the participants, personnel from other departments may be invited to attend as well, when the topic of discussion is relevant to their area of responsibility. Advisers in cities where informal discussion group meetings are not available might consider starting meetings with their local colleagues.

Advisers that have not yet fully developed the training component of

their compliance programs can use the ideas discussed in this article as a catalyst for doing so. Advisers that already have a training plan might use these ideas as part of their on-going effort to evolve, update and improve. □

1. See the NASD's Continuing Education Requirements in Membership and Registration Rule 1120, which became effective July 1, 1995.
2. Rule 206(4)-7 under the Investment Advisers Act of 1940 (the Advisers Act compliance rule) was adopted in 2003, with a compliance date of October 5, 2004.
3. SEC Release Nos. IA-2204; IC-26299, "Compliance Programs of Investment Companies and Investment Advisers," (Dec. 17, 2003) at Section II.C.1.
4. See Rule 206(4)-7(c).
5. To paraphrase Gene Gohlke from the SEC Staff in various remarks he has made publicly.
6. In appropriate cases, advisers may be held liable for failing to supervise their personnel as well.
7. Although in some circumstances, employees may be entitled to indemnification from their employers for losses or liabilities they incur in the course of their employment, indemnifications are by their terms subject to limitations and, in any event, regulators are insisting with increasing frequency that individuals waive their right to any indemnification (and insurance coverage) that might otherwise be available to protect them, as a condition to settling legal and enforcement actions.
8. This is similar to the two-part mandatory programs that broker-dealers are familiar with under NASD rules, which call for a "firm element" (annual firm-developed and administered training for all "covered persons") and a "regulatory element" (computer-based training for registered individuals). See NASD Membership and Registration Rule 1120.
9. Go easy on the chocolate, though.
10. Archived webcasts and other related materials are available at <http://www.sec.gov/info/ccoutreach.htm>.
11. Including the NSCP (program implementation expected later in 2007) and National Regulatory Services (NRS) in conjunction with the Investment Adviser Association.
12. Advisers should consider the appropriate handling and reporting of these arrangements, however, under the firm's gifts policy and soft dollar policies, particularly if resources are provided at no charge by outside vendors or brokers.

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