



Conducting an Annual Compliance Review

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Agenda

- Introduction to HedgeOp
- What Does the SEC Want to See?
- What Should an Annual Review Include?
- How to Document the Annual Review of Compliance Procedures
- Are There Any Tools that Can Help?
- Q&A

Introduction to HedgeOp

- HedgeOp provides varying levels of pro-active compliance support to over 35 different hedge fund and fund of fund firms with over \$50B in AUM. HedgeOp also provides project-based compliance support services and due diligence research and reporting services.
- HedgeOp has a staff of 32 people working in offices in NYC and Boston.
- The purpose of this seminar is to provide a summary of the annual review requirements of Advisers Act Rule 206(4)-7 and provide practical guidance on how to prepare for and conduct such a review. We also hope to provide insight on how innovative consulting tools from HedgeOp can provide practical assistance in meeting these regulatory requirements.

What Does the SEC Want to See?

- In addition to requiring the development of written compliance procedures and the appointment of a Chief Compliance Officer, Rule 206(4)-7 requires the following:
- “Review, no less frequently than annually, the adequacy of the policies and procedures established pursuant to this section and the effectiveness of their implementation”
- Any guidance in the Adopting Release? Not really, the Adopting Release for Rule 206(4)-7 provides in pertinent part:
- “The review should consider any compliance matters that arose during the previous year, any changes in the business activities of the adviser or its affiliates, and any changes in the Advisers Act or applicable regulations that might suggest a need to revise the policies or procedures”

What Should an Annual Review Include?

- Take and/or update the inventory of compliance obligations and issues applicable to your firm:
 - Access Person Reporting:
 - Personal transaction restrictions – use of restricted list
 - Pre-clearance requirements
 - Required Record-Keeping
 - Disclosure requirements:
 - Is all material information out there?
 - ADV updates
 - Consistency of various disclosure documents
 - Privacy policy procedures and controls
 - Trading related controls:
 - Best execution reviews
 - Trade or investment allocation policies
 - Use of soft dollars
 - Regulatory filings:
 - 13Ds, 13Gs, 13Fs
 - Section 16 filings
 - Hart-Scott Rodino filings
 - Updating of marketing and selling documents:
 - Offering memoranda, RFPs, marketing presentations

What Should an Annual Review Include?

- Review Conflicts of Interest in your business and how the conflicts are addressed by your firm:
 - Personal trading activities of employees
 - Any business with affiliated entities?
 - Do you trade through an affiliated broker? Is that disclosed to investors and clients?
 - Do you utilize any affiliated service providers? Is that disclosed to investors and clients?
 - How are trades and investment opportunities allocated?
 - Do you require employees to notify the firm of excessive gifts or business entertainment?
 - Do your personnel (or their families) have any affiliations with underlying investments?
 - Board representation, etc
- How does the firm address these conflicts?
 - Are they disclosed to investors and clients – where?
 - Do you seek consent for certain actions related to conflicts?

What Should an Annual Review Include?

- Critically review any compliance issues, Code of Ethics violations or other regulatory issues that occurred at your firm:
 - Any late or missing filings? What was the consequence to the particular Access Person?
 - Any failures to seek pre-clearance when required?
 - Any issues related to failure to seek compliance approval for marketing materials?
 - Any problems related to emails or safeguarding of electronic records?
 - Were the disaster recovery procedures tested? Any issues?
 - Did anyone share non-public information about investors with outsiders without obtaining consent?

What Should an Annual Review Include?

- Make inquiries of all of your employees as to possible compliance issues, problems or questions:
 - Do you understand your obligations under the Compliance Manual and other procedures?
Do you have any questions?
 - Have you noted any possible violations or problems under the compliance procedures or Code of Ethics?

What Should an Annual Review Include?

- Require employees to annually re-certify their commitment to compliance procedures and Code of Ethics:
 - Document for files.
- Make inquiries with service providers:
 - Remind them about relevant compliance policies:
 - Safeguarding of non-public information about investors and secured disposal of that information.
 - Disaster recovery procedures.
 - Require them to notify you of any compliance issues at their firm.
 - Require them to certify that they are of the view that they have control procedures in place to properly serve a registered investment adviser.

What Should an Annual Review Include?

- Critically review the internal testing and reporting that is done by your firm as to compliance obligations.
- Review whether your firm has engaged in any new business activities during the last year – what are the activities and what additional procedures were needed to address the new procedures:
 - New funds or products? Any new or more attractive fee structures?
 - New affiliates? New owners? Have you disclosed?

What Should an Annual Review Include?

- Review whether there have been any new regulatory developments that may need to be addressed:
 - Any new rules, laws or regulatory issues?
 - Insider trading investigations at hedge fund firms (i.e., Galleon)
- CCO should also consider reviewing the following:
 - Compliance compensation and budget issues
 - Do you have what you need?
 - Educational and employment experience of compliance personnel
 - Do you have what you need?
 - Her or his view on adequacy of procedures

How to Document the Annual Review

- Need for internal records related to annual review:
 - Advisers Act Rule 204-2 provides:
 - *“any records documenting the investment adviser’s annual review of those policies and procedures conducted pursuant to 206(4)-7(b)...”*
- LOTS of ways to comply – formal and informal.
 - Annual review memorandum with exhibits is probably the easiest way to go (based upon our experience here at HedgeOp).

Are There Tools That Can Help?

- Key to annual review process is **STAYING ON TRACK OF PROCESS and ORGANIZATION!!**
- Lots of options – do it yourself or utilize technology to facilitate, track and organize the annual review process.
- One option is ComplianceTrak

Are There Tools That Can Help?

- Calendar
 - Reporting
 - Task documentation
 - Archiving of evidence of compliance output
- Compliance Review Reports
- Conflicts of Interest Review Platform

Questions & Answers

- Thanks for your interest.
- Check www.hedgeop.com for info about our next webinar

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