



COMPLIANCE UPDATE

Final Rule: Compliance Programs of Investment Companies and Investment Advisers

Release Date: December 17, 2003

Effective Date: February 5, 2004

Compliance Date: October 5, 2004

On December 3, 2003 the SEC voted to adopt a new rule requiring Investment Companies and Investment Advisers to adopt comprehensive written policies and procedures reasonably designed to prevent violation of the federal securities laws. In particular, an adviser's policies and procedures must be designed to prevent violations of the Adviser Act by the adviser and its supervised persons. Here is a highlight of the requirements for Investment Advisers:

- Advisers must adopt written compliance policies and procedures that
 - are *reasonably* designed to prevent violations,
 - detect violations of securities laws, and
 - correct promptly any material violations.
- Advisers must review these policies and procedures at least annually to determine their adequacy and the effectiveness of their implementation.
- Advisers must designate a Chief Compliance Officer who will be responsible for administering the compliance policies and procedures.
 - The chief compliance officer should be competent and knowledgeable regarding the Advisers Act and should be empowered with the full responsibility and authority to develop and enforce appropriate policies and procedures for the firm. The compliance officer should have a position of sufficient seniority and authority within the organization to compel others to adhere to the compliance policies and procedures.
- Advisers must keep records documenting their annual review.
- Advisers must keep these records for five years, thus providing an examiner with the basis to determine whether the adviser has complied with the rule.

The Commission recognizes that advisers are too varied in their operations and therefore the rule does not impose a specific list of items that must be addressed in the policies and procedures. However, the Commission does suggest in its release that, to the extent relevant, the adviser's policies and procedures, at minimum, address:

- Portfolio management processes, including allocation of investment opportunities among clients and consistency of portfolios with guidelines established by clients, disclosures by the adviser, and regulatory restrictions;
- Trading practices, including procedures by which the adviser satisfies its best execution obligation, uses client brokerage to obtain research and other services ("soft dollar arrangements"), and allocates aggregate trades among clients;
- Proprietary trading of the adviser and personal trading activities of supervised persons;
- The accuracy of disclosures made to investors, including information in advertisements;
- Safeguarding of client assets from conversion or inappropriate use by advisory personnel;
- The accurate creation of required records and their maintenance in a manner that secures them from unauthorized alteration or use and protects them from untimely destruction;
- Marketing advisory services, including the use of solicitors;
- Processes to value client holdings and assess fees based on those valuations;
- Safeguards for the privacy protection of client records and information; and
- Business continuity plans.

Compliance Date: On or before the compliance date, all advisers must have designated a chief compliance officer and adopt compliance policies and procedures that satisfy the requirements in the new rules. Advisers must complete their first annual review of the compliance policies and procedures no later than eighteen months after the adoption or approval of the compliance policies and procedures.

Although the rule requires only annual reviews, the Commission expects that all registered advisers will begin reviewing their policies and procedures in light of the Commission's adoption of these new rules. Additionally, the Commission estimates in its release that it will take advisers on average 80 hours to document their policies and procedures that make up their compliance program.

For further clarification on how these changes affect you or for assistance in complying with the new rule, please contact:

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Please refer to the Commission's release on how the new rule affects Investment Companies:
<http://www.sec.gov/rules/final/ia-2204.htm>