

Suggestions to improve your approach to compliance program

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The most difficult aspect of testing could be documenting what you do, so consider this outline as a guide:

Briefly describe the test.

Bullet-point the items tested.

Describe major or problematic findings.

State how and when these problems were addressed.

David Hunt, deputy CCO at **NFJ Investment Group** in Dallas, uses a cover-sheet template he devised [[Tool Alert](#)]. It includes test results, follow-up actions and who completed the test, among other data. Hunt shared his approach during **IA Week**'s webinar last week on forensic testing.

Speakers talked about the difference between transactional testing and forensic testing. The latter examines topics over time. For example, you could do a random check to see if staff have reported gifts and entertainment that exceed your policy's limits. A one-time transactional test may not uncover a violation while a forensic test over time could add up all gift reports and flag an employee who topped your firm's annual limit on the value of gifts.

If you don't do much testing, start small, be inquisitive and you'll see your program grow over time, Hunt added. Focus on your firm's high-risk areas - ones that carry the most regulatory, reputational and financial risks. A rule-of-thumb he employs is the greater the risk, the more frequent the test.

Make sure you define what would be considered a major finding before you begin any test. "If you don't know what you're looking for before you start testing, you could pass right over it and never even know it," Hunt said.

There are transactional tests (e.g., involving trading) and quality control inquiries. Examples of quality control tests may be checking if your marketing materials were approved prior to release or whether client contracts were signed by an authorized person at your firm.

When it comes to best execution, one test used by **Verna Ramirez**, CCO at **Angelo Gordon and Co.** in New York, is randomly selecting 10 trades and comparing the firm's execution with **Bloomberg**'s volume weighted average price (VWAP). "If you're buying, you want the VWAP to be higher than your execution price, and if you're selling, you want the VWAP to be lower than your execution price," she says.

Another one of her favorite tests examines whether the firm charges expenses in line with its customer agreements. This includes confirming that a single expense has been fairly allocated across multiple accounts and reviewing the general ledger and other records to document expenses.

She also mentioned she uses a product ([Websense](#)) to track all web sites employees visit - as one way to monitor for the presence of malicious rumors.

If your firm is examined, you should drop in the initial interview that your program includes forensic testing, suggested **Michelle Kennedy** of **Compass Compliance Services** in Greenville, S.C. During this first meeting, you want to convey three things to examiners:

1. Confidence in your internal controls.
2. The impression that you're doing competent testing and monitoring of your policies and procedures.
3. That senior management is committed to compliance ("tone at the top").

"Just kind of relate to the SEC that what you're doing and what they're doing is one in the same," Kennedy said. It has been her experience through numerous exams that these impressions cut the time examiners spend on site and result in fewer deficiencies.

If you'd like to purchase the audio CD-ROM and working materials from this webinar, click [here](#).

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