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## A good compliance test: Can your vendor rapidly share records requested by the SEC

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Whether it's an e-mail, proxy service, portfolio management, document repository or some other vendor, your firm likely turns to a third-party to house key records. Recent SEC document request letters make clear that examiners will ask for records that may be held by these third-parties. Are you confident they could produce them quickly enough?

You could test their nimbleness by asking your vendors for certain records that ultimately could be requested by the SEC. And you can use your contract to enforce such swiftness. An SEC [no-action letter](#) from 2009 approves the use of such third-party vendors but stipulates conditions, such as that the records must be available to the adviser at any time, points out **Michelle Kennedy**, president of **Compass Compliance Services** in Greenville, S.C. ([IA Watch](#), Aug. 24, 2009).

Of course, the [books and records rule](#) requires records to be "in an easily accessible place for a period of not less than five years ... the first two years in an appropriate office of the investment adviser."

The adviser itself can be challenged to quickly retrieve requested documents for examiners. Kennedy counsels that you should periodically peruse a recent exam document request letter and test your ability to gather the records "promptly and accurately." Faulty CRMs or portfolio management software may contain the necessary data but not be set up correctly to permit ready access to it, such as lists of clients for whom the firm does and doesn't have discretion, account objectives or types of accounts offered, she adds.

"It is an incredibly time-consuming task to pull all of this data," she says. And "this is [the information examiners] want before they come in."

Take [this segment](#) of a recent exam letter. Among the items it seeks that could challenge advisers are whether each account is either an individual one, defined-benefit retirement plan, registered fund or unregistered fund. Your systems may capture this information but the data may be too dispersed for easy retrieval, Kennedy warns.

## Records of trades

Another delivery concern ties back to the trade blotter. This [SEC request](#) displays the preferred layout for the trade blotter. Kennedy notes that each transaction should have a broker associated with it. Code transactions, such as capital changes and dividend reinvestments, because the SEC may wish to segregate the data to view the buys and sales separately from other transactions, she recommends.

Other examples of data requested by the SEC that you may be challenged to produce quickly include whether an adviser's affiliate acts as a trustee, the investment strategy and related performance composite, commission recapture in directed brokerage arrangements and custody.

This recent [SEC exam letter](#) demonstrates again the agency's interest in custody (see [related story](#)). It asked the adviser for records related to "whether or not the custodian sends production account statements directly to the client; whether or not the delivery is electronic, if so, a copy of the authorization; and the form of electronic delivery (e.g., email or website login)."

Another example of relying upon a vendor can be seen in the letter's request that the adviser ask its custodians to "provide an acknowledgement that it sends account statements directly to clients (rather than solely to the Adviser) at least quarterly and provide the names of these clients." Examiners ask the adviser to request that the custodian provide its answers directly to the SEC.

This [new document request letter](#) sparks interest because it appears to be a mix of a so-called "presence exam" and a routine inquiry. Some noteworthy selections ask the adviser to "label" its production to correspond to the item number in the SEC's request list, a list of securities whose values came from a pricing service but were overridden by the adviser, a trade blotter covering the entire exam period and a list of commission-sharing arrangements.

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