



Perspective

Industry Focused News

Vista360 Perspective mailings are intended to provide advisers and funds with snapshots of current industry topics and news we believe to be noteworthy. This issue of Vista360's Perspective includes:

- [Proposed Amendments to the Custody Rule \(5/14/09\)](#);
- [Sample SEC Exam Request Language – Custody Documents](#); and
- [Highlights from the Regulators' Panel Discussion at NSCP's Chicago Meeting \(4/20/09\)](#).

To read past issues of the Perspective including Vista360's most recent quarterly Hot Industry Topics List, [please visit our web site](#).

Proposed Amendments to the Custody Rule

On May 14, 2009, the SEC proposed amendments to the Custody Rule, with the objective of strengthening controls required by advisers who maintain custody over client assets. The SEC requested comments on the following proposals:

- A yearly "surprise exam" of all registered investment advisers with custody of client assets by an independent public accountant.
- New reporting requirements include:
 - The adviser must disclose in public filings the identity of the accountant performing the surprise exam; and
 - The accountant must report any material discrepancies uncovered during their exams to the SEC.
- If an adviser has client authority to access funds, or if the adviser is affiliated with the custodian, a custody control review must be conducted by a PCAOB-registered accountant. The adviser must obtain a written report that includes:
 - A description of the custody controls in place;
 - The tests performed of the effectiveness of the controls; and
 - The results of the tests performed.
- All custodians must send statements directly to advisory clients, rather than through the investment adviser.

We anticipate quite a bit of pushback from the industry on the proposal to require independent accountant reviews if an adviser has access to client funds only for purposes of withdrawing fees.

Custody Exam Request Letter

As you may know, the SEC is currently conducting exams of certain investment advisers regarding the custody of their clients' assets. The goals of the exams are for SEC staff to better understand the adviser's custodial arrangements, the controls in place for the safekeeping of client assets, and the implementation of the controls. Advisers who are subject to one of these exams are expected to make those personnel available who can answer questions and explain the aspects of an adviser's custody controls. We have also observed the SEC is including these custody requests within routine examinations.

In recent exams, the document request list includes the following language regarding custody:

Please request that the Custodian(s) 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 (if this is an accurate statement). The Custodian should send the acknowledgment directly (to the SEC).

Also, please be aware that after the on-site examination begins, the staff may further ask the Adviser to request the Custodian(s) to provide a confirmation of all positions, including cash, short positions and loans, held as of a particular date for specific clients.

Heard at the NSCP – Regulators' Voice

Vista360 attended the National Society of Compliance Professionals, Inc. ("NSCP") Midwest Regional Meeting in Chicago on April 20th. Summarized below are comments we found interesting from Jane Jarcho of SEC's Chicago Regional Office and Rosemary Hollinger of CFTC's Central Regional Office. For more information on where the SEC is focusing its resources, please read Lori Richards' [speech](#) from the IA Compliance Best Practices Summit 2009.

➤ ***SEC and CFTC Staff Comments***

- Ms. Jarcho and Ms. Hollinger noted the SEC and the CFTC have and will continue to increase communication with one another, regardless of whether a formal merger between the agencies transpires in the future.
- Their cooperation is necessary in overlapping jurisdictions, especially when working with hedge funds.

➤ ***SEC Examinations***

- **Key Areas of Focus**
 - Custody of client assets
 - Performance
 - Compliance programs and resources
- **Types of Exams and Exam Frequency**
 - SEC's exam cycle will be **atypical** in 2009.
 - Sweep exams currently underway are focusing on custody and performance.
 - Expect more sweep-type exams during 2009.

- Risk-based exams (high – 3 years, medium – 5 years, low – 10 years)
- Cause exams are based on any complaints or tips, which the SEC estimates at 1.6 million per year.
- **Document Requests:** The SEC staff urged advisers to communicate any delivery delays following an SEC request for documentation.
- **Enforcement:** The SEC is focused on enhancing the Division of Enforcement in the following ways, which should result in faster turnaround of cases, and more enforcement actions against fraudulent or deceptive practices:
 - New Director – Robert Khuzami (former federal prosecutor)
 - Revamping handling of tips and complaints
 - Hiring individuals with specialized skill sets
 - Current investigations
 - Ponzi schemes
 - Municipal securities
 - Credit default swaps, CDOs and other derivative related investments

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