

## Points of Emphasis/Best Practice Summary

If you are a mid-sized adviser no longer eligible for SEC registration that needs to transition to state registration, that process needs to begin as soon as possible if you have not begun the process of switching already. What is a “mid-sized adviser”? A mid-sized adviser is an investment adviser that has between \$25 million and \$100 million of assets under management. Most mid-sized advisers must transition to state registration no later than June 28, 2012. As a reminder, every adviser registered with the SEC on January 1, 2012 must file an amendment to its Form ADV no later than March 30, 2012. For advisers with a December fiscal year end, this will be accomplished with the filing of your annual updating amendment.



CMC stands ready to assist all of our mid-sized adviser clients with state transition process.

After filing the Form ADV amendment, mid-sized advisers no longer eligible for SEC registration must submit an application for registration in the state in which it maintains its principal office and place of business, and withdraw their SEC registration by filing a Form ADV-W no later than June 28, 2012. The SEC will cancel the registration of advisers no longer eligible to register with the SEC that fail to file an amendment or withdraw their registrations in accordance with the rule. Firms should submit state applications and obtain approval prior to withdrawing their SEC registration to avoid any lapse in registration.

In addition to registering in the state in which the

firm maintains its principal office and place of business, firms should also register in other states in which it has customers and does not meet the state's de minimis exemption, and/or in states in which it has customers and the state does not follow a de minimis rule. Firms are encouraged to check the registration requirements for all states in which it maintains customers as not all states follow the national de minimis rule. In addition, some states follow the national de minimis rule but still have certain requirements if you maintain customers in their state.

## Regulatory Corner

The SEC has issued proposed rule, “Regulation S-ID: Identity Theft Red Flags,” requiring entities that are subject to the SEC’s jurisdiction to develop and implement a written identity theft prevention program that is designed to detect, prevent, and mitigate identity theft. The SEC is also proposing guidelines to assist these entities in the formulation and maintenance of a program that would satisfy the requirements of the proposed rules. The proposed rules and guidelines are substantially similar to the Fair and Accurate Credit Transactions Act of 2003, which was adopted in 2007. Among other financial institutions included in the scope of Regulation S-ID, an investment adviser that is registered or required to be registered under the Investment Advisers Act of 1940 will be subject to the proposed rules.

The definition of “financial institution” includes certain banks and credit unions and “any other person that, directly or indirectly, holds a transac-

tion account (as defined in section 19(b) of the Federal Reserve Act) belonging to a consumer.” Section 19(b) of the Federal Reserve Act defines a transaction account as “a deposit or account on which the depositor or account holder is permitted to make withdrawals by negotiable or transferable instrument, payment orders of withdrawal, telephone transfers, or other similar items for the purpose of making payments or transfers to third parties or others.” The SEC recognizes that most registered investment advisers are unlikely to hold transaction accounts and thus would not qualify as financial institutions. The proposed definition nonetheless does not exclude investment advisers or any other entities regulated by the SEC because they may hold transaction accounts or otherwise

meet the definition of “financial institution.”

The SEC acknowledges that some financial institutions may engage only in transactions with businesses where the risk of identity theft is minimal.

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In these instances, the financial institution may determine after a preliminary risk assessment that it does not need to develop and implement a program. Under the proposed rules, a financial institution or creditor that initially determines that it does not need to have a program would be required to periodically reassess whether it

must develop and implement a program in light of changes in the accounts that it offers or maintains and the various other factors set forth in the proposed rule.

## Word on the Street

The SEC’s Office of Compliance Inspections and Examinations has issued a National Examination Risk Alert concerning investment adviser use of social media. Investment advisers are increasingly utilizing social media outlets to communicate with existing and potential clients, promote services, educate investors and recruit new employees. Firms’ use of social media must comply with various provisions of the federal securities laws, including, but not limited to, the antifraud provisions, compliance provisions, and recordkeeping provisions. Firms using social media should adopt, and periodically review the effectiveness of, policies and procedures regarding social media. The SEC evaluated registered investment advisers of varying sizes and strategies



Ensure your compliance manual addresses the use of social media. Contact CMC today if you need to update your procedures.

that were using social media to evaluate whether their use complied with the federal securities laws.

Factors that might be considered when adopting and reviewing the effectiveness of policies and procedures concerning the use of social media

include usage guidelines, content standards, sufficient monitoring, approval of content, training, etc. Particular attention should be paid to third party content (if permitted) and record-keeping responsibilities. In their Alert, the SEC noted that they had observed that many firms have multiple overlapping procedures that apply to advertisements, client communications or electronic communications generally, which may or may not

specifically include social media use. The SEC indicated that such lack of specificity may cause confusion as to what procedures or standards apply to social media use. In addition, many procedures were not specific as to which types of social networking activity are permitted or prohibited by the firm and many did not address the use of social media by solicitors.

Firms should consider reviewing their record retention policies to ensure that any required records generated by social media communications are retained in compliance with the federal securities laws, including in a manner that is easily accessible for a period not less than five years. In addition, firms must ensure that they are in compliance with all of the regulatory requirements and be aware of the risks associated with the use of various forms of social media.