

The cost of ignoring compliance

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“If you think compliance is expensive, try non-compliance” – Paul McNulty, former US deputy AG

In today’s increasingly automated, fast-paced world, companies must ensure that their legal and regulatory reviews are accurate, efficient, and risk-averse. When a company fails to adopt compliance practices, the chances of being penalised are higher. Investment advisers have to be careful to adhere to regulations when marketing their financial products to prospects/clients.

In this blog, we discuss some compliance best practices and present an actual case that shows the importance of having a strong compliance framework in place.

The Office of Compliance Inspections and Examinations (OCIE) lists the prominent reasons for the violation of compliance issues not limited to:

- Misleading performance results
- Misleading one-on-one presentations
- Claiming compliance with voluntary performance standards
- Cherry-picked profitable stock selections
- Misleading selection of recommendations
- Compliance policies and procedures

Analysis of a recent case gives us a broader view of potential compliance violations:

A Boston-based investment adviser was fined USD 1m for failing to comply with advertising and compliance guidelines. According to the SEC’s order, the company allegedly distributed misleading marketing materials related to its historical performance. It was found that the materials represented the company as directly managing an investment, when in fact, it was an investment in a private fund advised by a third party.

Furthermore, by including the private fund’s performance, the investment adviser misleadingly improved its investment track record. It was unsuccessful in implementing the policies and procedures contained in its compliance manual vis-à-vis the use of investment performance results in its marketing materials. It violated Section 206(4) of the Investment Advisers Act of 1940 and

Rules 206(4)-1 and 206(4)-7 therein.

Both the rules apply only to investment advisers registered with the SEC; under rule 206(4)-1, investment advisers are prohibited from using any advertisement that contains an untrue statement of a material fact or that is otherwise misleading.

Under rule 206(4)-7, investment advisers are prohibited from providing investment advice unless the adviser has adopted and implemented policies and procedures designed to thwart a violation of the Advisers Act by the adviser. This rule requires the advisers to consider their fiduciary and regulatory obligations under the Advisers Act and to reinforce the policies and procedures to address them.

It is unlawful for an investment adviser registered under Section 203 within the meaning of Section 206 to provide investment advice to clients unless

(a) Policies and procedures: You have to adopt and implement written policies and procedures designed to prevent violation of the Act and the rules that the SEC has adopted under the Act;

(b) Annual review: You have to perform frequent reviews, at least annually, of the appropriateness of the policies and procedures established under this section and the effectiveness of their implementation; and

(c) Chief compliance officer: You have to designate an individual who will be responsible for overseeing the policies and procedures that you adopt, as mentioned above in section (a).

The most effective shield against such incidents is having adequate policies in place and not failing to implement them.

Thus, a company can safeguard itself, but only by adhering to compliance regulations.

Fines and sanctions do not only cost companies money, but also affect their **reputation, goodwill, and trust with stakeholders.**

These challenges can be mitigated by

- establishing effective compliance policies and procedures
- forming a robust training system to distinguish between ethical and unethical practices
- having a marketing and distribution compliance manual
- creating a dedicated team of experienced personnel to conduct reviews

Companies also need to look at marketing materials from the end users' (i.e., the audience's) point of view. Marketing compliance reviewers should ensure that the business analysts show performance numbers or other performance-related information in line with regulations.

Marketing compliance reviewers check whether the communication is fair and balanced, and not misleading to investors. They also watch for regulatory updates to mitigate possible risks.

It is never too late for a company to review its policies and procedures, and to have an effective marketing compliance team that can help mitigate risks.

Good will and a good reputation are two of the most valuable assets a company can have.

How Acuity Partners can help:

Acuity is equipped with personnel who have knowledge and experience in the field of marketing compliance, these professionals can help you safeguard your company from violating any guidelines set in place by the regulators. We also focus on thought leadership and understand compliance requirements based on different jurisdiction. Acuity has multi-functional [compliance support](#) which can enable you to reduce overall compliance costs.

Sources:

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We empower our clients to drive revenues higher. We innovate using our proprietary technology and automation solutions. We enable our clients to transform their operating model and cost base.