

INVESTMENT ADVISER **Compliance Update**

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A complimentary service to our clients

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I. REMEMBER: COMPLIANCE IS AN ONGOING PROCESS

Please remember that compliance is an ongoing and constantly evolving process. Laws and rules applicable to your practice and representatives are subject to change. Agreements and disclosure statements may require review and update due to regulatory or state law changes and/or changes in your business operations. Existing restrictive covenant agreements may no longer reflect state law changes. Please do not become complacent with respect to compliance matters. The scope of SEC examination issues continues to grow and becomes more complex. Policies and Procedures must also be reviewed and revised as required by regulatory changes and/or changes in your business operations. A ripe area for SEC deficiencies is either failure to have Policies and Procedures that appropriately reflect your business operations and/or the failure to follow them. As always, we will continue to remain available to assist with these matters.

II. RISK AND THE RIA – Are you Prepared for the SEC’s New Examination Request List?

As any RIA who has been through a recent SEC examination can attest, the SEC’s latest document request lists takes a “one size fits none” approach by requiring the production of many items that are unfamiliar or inapplicable to most investment advisers. While many of these items are not required by the Adviser’s Act, RIAs are well advised to comply with the requests rather than face the possibility of longer, more frequent SEC inspections.

Some of the items requested that have caused the most confusion for RIAs include questions regarding the “risk management process.” Most investment advisers tend to think about risk in terms of investments and portfolio management. However, the SEC items that require the production of risk-related documents focus on operational and compliance risks. For example, one section requires the production of the adviser’s Standard Operating Procedures for the risk assessment process, a matrix or spreadsheet that maps the adviser’s inventory of risks, and the adviser’s most current inventory of risks.

We advise RIAs to establish policies and procedures to assess the risks of compliance and operational weaknesses. Such procedures should encompass, at a minimum, the ten major areas that RIAs are required to address pursuant to Rule 206(4)-7. Documenting the risk-related items requested by SEC examiners requires time and discipline. In order to draft appropriate procedures, all employees of the RIA should be encouraged to: (1) analyze the operational areas over which they are responsible; (2) document possible areas of risk; and (3) suggest policies and procedures to mitigate such risks.

We remain available to assist with these matters.

III. MEETING THE NASD’S DEADLINE FOR BRANCH OFFICE REGISTRATION

In October 2005 the NASD’s new “uniform definition” of a Branch Office became effective. As part of the new “uniform definition” process Broker/Dealer firms will be obligated to assess their supervisory structure, determining whether any current places of business constitute a “branch office” or whether they constitute non-branch “unregistered locations.” Places of business deemed to be “branch offices” will need to be registered on the newly created Uniform Branch Office Registration Form (Form BR) on NASD’s CRD system. NASD, the NYSE, and the North American Securities Administrators Association (NASAA) collaborated in developing the Form BR to enable

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firms to register branch offices electronically with NASD, the NYSE, and the several states that require “branch office” registration. Form BR replaces Schedule E on Form BD (as well as the NYSE Branch Office Application Form and the forms used by states to register branches.) Filing the Form BR via Web CRD is intended to streamline the branch registration process for NASD member firms. Firms will have until **July 3, 2006** to comply with a number of filing requirements. Firms will need to file an amended Form BR for each converted branch. Firms will also need to assign registered persons to a registered branch office or the main office locations from which they work. Should you have any questions about whether a place of business is a “branch office” requiring registration on Form BR or whether any of your current places of business are “unregistered locations” exempt from registration on Form BR, call us here at *Stark & Stark*. We can also assist you in completing your Form BR prior to the July 3rd deadline.

IV. 13F – DOES IT APPLY TO YOU?

An investment adviser with \$100 million of qualifying 13(f) securities under its discretionary management (*see* below) must file a Form 13F. The initial 13F filing is due by February 14th following the initial year when the assets under management first reach \$100 million. Thus, if the adviser first reaches \$100 million on the last trading day of the calendar year (e.g. 12/31/05), the initial 13F filing is required by February 14th of the following year (e.g. 2/14/06). Thereafter, a Form 13F filing is required within 45 days after the end of each calendar quarter. The timing for discontinuing 13F filings would be the last quarter of the calendar year subsequent to the calendar year in which the adviser no longer has \$100 million in qualifying 13(f) discretionary assets under its management. Thus, if on December 31, 2005, an adviser’s qualifying discretionary assets dipped below \$100 million, and remained below \$100 million during the entirety of 2006, the last required filing would be due on February 14, 2007.

When determining if it has \$100 million in “13(f) securities,” the adviser should count all assets representing equity securities that are admitted to trading on a national securities exchange or quoted on the automated quotation system of a registered securities association. The term “equity security” means any equity security of a class which is registered, or any equity security of any insurance company which would have been required to be so registered except for an exemption, or any equity security issued by a registered closed-end investment company (this includes closed-end mutual funds). An adviser can confirm if it has \$100 million in 13(f) securities by cross-checking the securities that the firm manages with those on the 13(f) list published by the SEC on a quarterly basis: <http://www.sec.gov/divisions/investment/13flists.htm>. In addition, if the adviser has discretion to allocate assets among sub-advisers, the securities purchase by these sub-advisers may need to be included when determining if the adviser has reached the \$100 million threshold.

Once the adviser determines that it has \$100 million of 13(f) securities, the firm should then register with EDGAR. While the EDGAR registration process is underway, it is prudent to begin the compiling and formatting the required 13(f) securities information.

We will continue to remain available to assist with 13F filings.

V. RULE 206(4)-7 ANNUAL REVIEW – APRIL 2006 DEADLINE

Please remember that pursuant to the requirements of Rule 206(4)-7, all advisory firms must have completed an initial annual review of its compliance policies and procedures by April 6, 2006. The purpose of the review is to ascertain the extent to which the firm’s current policies, as well as the procedures implemented to effect the policies, require amendment. The review should be conducted by the Chief Compliance Officer, or his/her designee, who should consider the following four items in addition to other relevant issues:

- Compliance matters that arose during the previous year;
- Changes in the advisory firm’s business;
- Changes in the activities of any of the firm’s advisory affiliates; and,
- Changes in the regulations applicable to the advisory firm, including changes to the Investment Advisers Act of 1940, and Rules promulgated thereunder.

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This annual review requirement must be memorialized in an organized and coherent manner. To the extent that your firm requires any assistance with this requirement or is interested in obtaining an annual review form, please contact our office.

VI. HAS YOUR CLIENT SUFFERED LARGE LOSSES AT ANOTHER FIRM?

So often, clients seek to change investment professionals after having suffered losses they did not have to incur. Stark & Stark can help. Our Securities Arbitration Practice Group, which customarily defends investment industry professionals, will review and pursue customer claims when referred to us by our investment professional clients. We do limit this representation to substantial cases, usually involving \$500,000 or more in damages.

VII. RIA BRANCH OFFICES AND FORM BR

SEC and state registered investment adviser firms with branch offices in representative jurisdictions are now required to file a Form BR and update the individual adviser Form U-4. The deadline for Form BR filings is May 2006. If you have a branch office consistent with the relevant chart below, contact Stark & Stark, so we can ensure the proper filings occur.

If a firm is **state registered** in one of the following jurisdictions a Form BR is required (in addition to U-4 amendments):

- i. Connecticut
- ii. Florida
- iii. Maine
- iv. Nevada
- v. Texas
- vi. West Virginia
- vii. Vermont

If the firm is SEC registered and **noticed filed** in one of the following jurisdictions, a Form BR must be filed (in addition to U-4 amendments):

- i. Alabama
- ii. Hawaii
- iii. Idaho
- iv. Illinois
- v. Indiana
- vi. Kansas
- vii. Michigan
- viii. New Mexico
- ix. Ohio
- x. Rhode Island
- xi. South Dakota
- xii. Tennessee
- xiii. Wisconsin

VIII. STATES ADOPT SEC POLICIES AND PROCEDURES RULE

Please note that many states now require state registered investment advisers to comply with SEC Rule 206(4)-7. Because we fully expect the vast majority of states to adopt the Rule, we strongly recommend that all registered investment advisers comply with the SEC Rule at this time. Compliance requires advisers to (i) adopt policies and procedures designed to prevent violations of applicable securities laws, including the Investment Advisers Act of 1940; (ii) annually review their established policies and procedures for their adequacy and the effectiveness of their implementation; and (iii) designate a chief compliance officer responsible for administering the policies and procedures. To the extent that you require any assistance or have any questions, we will remain available to assist you.

If you are a state registered investment adviser and have not yet implemented written policies and procedures, please make contacting Stark & Stark a priority in order to confirm the extent of the relevant state's adoption of the SEC's written policies and procedures requirement.

IX. RECEIVE IMPORTANT NEWS AND COMPLIANCE UPDATES VIA RSS

We are always striving to provide our clients with tools to make receiving information important to them as easy as possible. Accordingly, we have recently made available a RSS (really simple syndication) feed through which we will distribute our Compliance Update Newsletter, client alerts, and news about important industry developments.

Subscribing to our RSS feed allows you to receive news and updates from us in a convenient and simple manner. Using RSS frees you from constantly revisiting our website to see what new information has been added since your last visit. Receiving updates via RSS also helps to keep your desk clear of hard copy mailings and reduces the amount of email alert messages coming into your inbox.

RSS feeds are read in a program called an aggregator. This aggregator program runs invisibly and only notifies you when new information has been published through the feed. There are many choices of aggregators for you to use, and we have included a list of them below.

RSS is a relatively new technology that has the potential to revolutionize how businesses communicate in the same way that email has. Realizing the potential of RSS, we encourage our clients to become involved by subscribing to our feed and experiencing for themselves this simplified method of communication.

It is important to note that we will still continue to provide information to you in hard copy form, including client alerts and compliance updates, until you direct otherwise. The main benefit, though, of subscribing to our RSS feed is that you will receive this information on your computer the instant we publish it, and will no longer have to sort through your inbox or shuffle papers on your desk.

Should you have any questions regarding RSS technology and how it can be used, please contact our Director of Business Development Richard DeLuca at rdeluca@stark-stark.com or 609-791-7014. He regularly provides advice on RSS technology to Stark & Stark clients.

Securities Compliance & Arbitration RSS Feed

<http://www.njlawblog.com/feed-wbsecuritiesblogpostings.rdf>

Aggregators That Can Be Used to Receive RSS Feeds

Abilon - <http://www.activerefresh.com/abilon/>

Displays headlines from RSS Channels in an easy to read format. It is a small, fast, and free program. Adding new channels is as simple as right-clicking and entering the address of the feed.

FeedDemon - <http://www.bradsoft.com/feeddemon/>

Enables you to quickly explore the world of RSS from your desktop without having to visit hundreds of sites. FeedDemon makes RSS as easy to access as your email.

***This is the aggregator program used by Stark & Stark.**

Additional aggregators for Windows based operating systems can be found here -

<http://allrss.com/rssreaderswindows.html>

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Remember, compliance is an ongoing and constantly evolving process. In that regard, Stark & Stark continues to remain available, at your convenience, to assist you relative to the applicability of any of the above issues to your specific practice. As always, we can be reached directly by telephone or e-mail as listed below.



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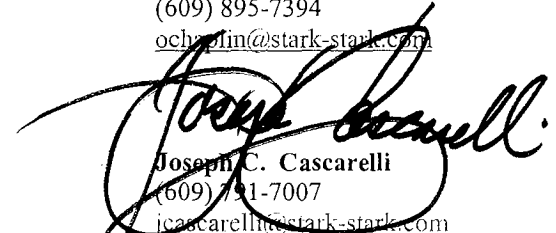
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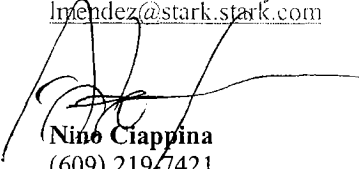
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