

bullet point

a note from Tannenbaum Helpern Syracuse & Hirschtritt LLP

Registered Investment Advisers Are Now Expected to Retain E-mail¹

To: Clients and Friends of Tannenbaum Helpern Syracuse
Hirschtritt LLP

Date: March 22, 2004

The SEC Examiners Will Now Request Adviser's to Produce Their E-Mail

Are registered investment advisers required to adopt a formal e-mail retention policy is an often repeated question asked by fund managers. At the "SEC Speaks" conference sponsored by the Practising Law Institute, the staff of the Securities and Exchange Commission (the "SEC") emphatically stated that SEC investigators will request an adviser to produce its past e-mails when conducting an inspection of the adviser.² According to the SEC staff, the impetus for requesting past e-mail has been the market timing and late trading scandals involving mutual funds and hedge funds. The SEC staff stated that one of the factors leading to the SEC's discovery of late trading and market timing was by examining past e-mails of advisers. E-mail has become a useful tool in the SEC's efforts to detect fraud and wrongdoing. As such, requesting an adviser to produce its e-mails is now a standard request during an inspection.

Until the SEC staff publicly stated that advisers are to retain their e-mails, there has been some uncertainty as to whether registered investment advisers are required to maintain e-mail. What has perpetrated this uncertainty is the absence of a definitive statement in the form of an interpretive release from the SEC mandating registered investment advisers to adopt an e-mail retention policy pursuant to the recordkeeping rules under the Investment Advisers Act of 1940, as amended (the "Advisers Act")³. Adding to this perplexity has been the fact that other regulated financial entities are subject to e-mail retention rules. For example, the SEC has provided guidance for broker-dealers: in Release No. 34-38245, the SEC addressed the use of electronic communications and stated that the recordkeeping requirements described in Rule 17a-4(b)(4) of the Securities Exchange Act of 1934 apply to e-mail.⁴ Furthermore, financial firms registered with the Commodity Futures Trading Commission and the National Futures

¹ This memorandum provides general information on the subject matter described, and it should not be relied on for legal advice on any matter, which may turn on specific facts. You should seek specific legal advice before acting with regard to the subjects treated here.

² "The SEC Speaks" Conference, sponsored by the Practising Law Institute, Workshop on Compliance, Inspections and Examinations (March 6, 2004).

³ The types of documents to be maintained are described in Rule 204-2(a)(1)-(16), Rule 204-2(b), Rule 204-2(c), and Rule 204-2(e)(2) of the Advisers Act.

⁴ According to the SEC, "broker-dealers must retain only those e-mail and Internet communications (including inter-office communications) which related to the broker-dealer's 'business as such.'" See Release No. 34-38245 (January 31, 1997).

Association, e.g. commodity pool operators and commodity trading advisers, are subject to e-mail retention requirements.⁵

Develop an E-Mail Retention Policy

Now that it is clear that a registered investment adviser is to maintain an e-mail retention policy, an adviser should now develop and implement an e-mail retention policy. Such a policy should address the following:

- Identify what is to be preserved
- Identify what is to be deleted
- Determine how often e-mails will be archived, e.g. weekly, monthly, etc.
- Determine how far back a time period your firm will retain e-mail
- Determine the storage media to be used to preserve e-mail, e.g. tapes, CDs
- Will your firm recycle the storage media? If so, how often is the recycling rotation?⁶
- Will e-mail be maintained by a third-party vendor offsite?

An adviser's e-mail retention policy does not necessarily have to be a stand-alone policy. The e-mail retention policy may be incorporated within an adviser's general recordkeeping policy.

In terms of how long to retain archived e-mails, until the SEC issues further guidance, an adviser should retain e-mails in accordance with the current requirements under the Advisers Act. As such, archived e-mail should be retained for a period of five years, the first two years on-site at the adviser's office.⁷

After an e-mail retention policy is adopted, an adviser should circulate the e-mail retention policy to all employees.

Other Issues to Consider

Note that Rule 206(4)-7 of the Advisers Act will go into effect this October 5, 2004.⁸ Pursuant to Rule 206(4)-7, an adviser is required to implement a written compliance program that addresses *inter alia* recordkeeping.⁹ Now is a good time for an adviser to start formulating its general recordkeeping policy that should include a section that addresses e-mail retention.

⁵ Electronic communications, e.g. e-mail, are to be maintained in accordance with Rule 1.31 of the Commodity Exchange Act or in accordance with the SEC's guidance as described in Release No. 34-38245. See Commodity Futures Trading Commission; "Interpretation Regarding Use of Electronic Media by Commodity Pool Operators and Commodity Trading Advisors for Delivery of Disclosure Documents and Other Materials; final rule. 62 Fed. Reg. 39104-39115 (July 22, 1997).

⁶ Note that during the panel discussion in the Workshop on Compliance, Inspections and Examinations, the SEC took a critical position with an adviser that was examined which had retained e-mail on a tape for three month periods and would then recycle the tape.

⁷ In general, a registered investment adviser is required to maintain books and records with respect to its advisory services for a period of five years (the first two years on-site at the adviser's office) pursuant to Rule 204-2(e)(1) of the Advisers Act.

⁸ Securities and Exchange Commission; "Compliance Programs of Investment Companies and Investment Advisers"; final rule. 68 Fed. Reg. 74714-74730 (December 24, 2003).

⁹ See 68 Fed. Reg. at 74716.

Disaster recovery and business continuity is another component an adviser is to implement under Rule 206(4)-7.¹⁰ An adviser's disaster recovery and business continuity plan should also address the backing up of e-mail and the maintenance of archived e-mail offsite.

* * * * *

If you have any questions or comments on developing and implementing an e-mail retention policy, please feel free to contact:

Michael G. Tannenbaum
(212) 508-6701
tannenbaum@tanhelp.com

Ricardo W. Davidovich
(212) 508-6710
davidovich@tanhelp.com

Roderick J. Cruz
(212) 702-3149
cruz@tanhelp.com

Tannenbaum Helpern Syracuse & Hirschrift LLP
New York London
www.tanhelp.com

¹⁰ See 68 Fed. Reg. at 74716, note 22